

Prefatory Note

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Part 2

August 2, 2007

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

August 2, 2007

Recent Developments

Domestic Nonfinancial Developments

Domestic Nonfinancial Developments

Real GDP increased at an annual rate of 2 percent, on average, over the first half of the year; and, the drag from housing and the recent turbulence in financial markets notwithstanding, the available indicators taken as a whole are consistent with economic activity posting further moderate gains in the near term. In particular, employment and real income have been growing solidly, on balance, so far this year, indicators of household and business sentiment remain supportive, and inventories appear to be reasonably well aligned with final demand. Top-line inflation receded in June, while core inflation rose at about its average pace over the past year.

Labor Market Developments

Labor demand has continued to expand at a moderate pace. Private payroll employment rose 92,000 in June and was led by gains in the education and health services and in the leisure and hospitality industries. Construction employment also rose in June despite the ongoing contraction of activity in that sector, a continuation of the anomalous pattern observed since early 2007. For the second quarter as a whole, private payrolls increased an average of 115,000 employees per month, the same rate as in the first quarter. Reflecting the growth in payroll employment, as well as a small lengthening of the workweek, aggregate hours of private production or nonsupervisory workers rose at an annual rate of 2.3 percent in the second quarter.

In the household survey, the unemployment rate held steady at 4.5 percent in June and has been largely unchanged for nine months. The labor force participation rate edged up to 66.1 percent in June. The participation rate had increased between early 2005 and the end of 2006; since then it has been moving down, on average, although it is still above the level observed in early 2005.

Other gauges of labor demand have remained in a range consistent with continued moderate employment growth. Indicators of layoffs—such as initial claims for unemployment insurance, the short-term job losers rate from the household survey, the layoff and discharge rate from the Job Openings and Labor Turnover Survey, and announcements of downsizing plans—all suggest that job losses have been relatively subdued recently. On the hiring side, most measures of hiring plans, job openings, and job availability, although off a bit from recent peaks, remain at relatively high levels by historical standards.

Changes in Employment

(Thousands of employees; seasonally adjusted)

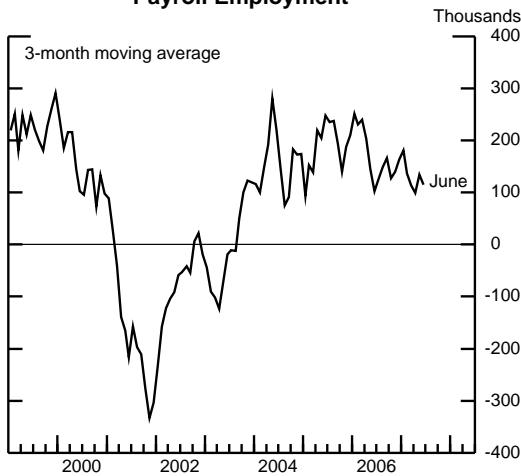
Measure and sector	2006	2007					
		Q4	Q1	Q2	Apr.	May	June
	Average monthly change			Monthly change			
Nonfarm payroll employment (establishment survey)	189	177	142	148	122	190	132
Private	169	164	115	115	90	163	92
Natural resources and mining	5	4	3	2	2	0	3
Manufacturing	-7	-25	-14	-14	-18	-7	-18
Construction	11	-14	3	-4	-21	-2	12
Wholesale trade	11	12	2	16	17	10	20
Retail trade	-3	11	27	-13	-27	13	-24
Transportation and utilities	9	11	2	2	0	0	7
Information	2	7	4	5	10	5	0
Financial activities	16	10	2	7	3	16	1
Professional and business services	42	52	14	13	25	22	-9
Temporary help services	-1	6	-7	-9	-8	-11	-8
Nonbusiness services ¹	83	96	71	102	98	106	101
Total government	20	13	28	33	32	27	40
Total employment (household survey)	262	340	109	-38	-468	157	197
Memo:							
Aggregate hours of private production workers (percent change) ²	2.5	2.0	1.1	2.3	-.2	.2	.5
Average workweek (hours) ³	33.8	33.9	33.8	33.8	33.8	33.8	33.9
Manufacturing (hours)	41.1	41.1	41.0	41.2	41.1	41.1	41.3

1. Nonbusiness services comprises education and health, leisure and hospitality, and "other."

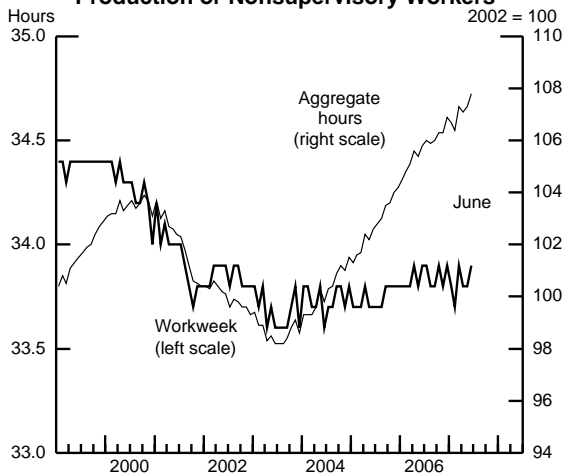
2. Establishment survey. Annual data are percent changes from Q4 to Q4. Quarterly data are percent changes from preceding quarter at an annual rate. Monthly data are percent changes from preceding month.

3. Establishment survey.

Changes in Private Payroll Employment



Aggregate Hours and Workweek of Production or Nonsupervisory Workers

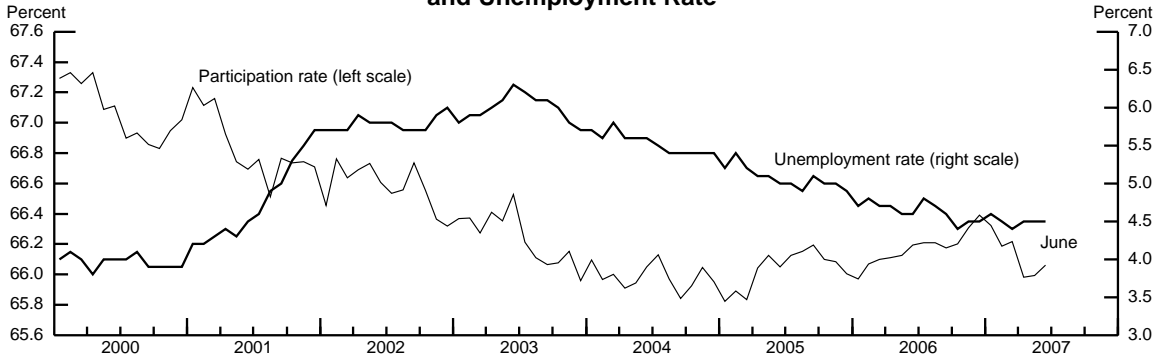


Selected Unemployment and Labor Force Participation Rates

(Percent; seasonally adjusted)

Rate and group	2006	2007					
		Q4	Q1	Q2	Apr.	May	June
<i>Civilian unemployment rate</i>							
Total	4.6	4.5	4.5	4.5	4.5	4.5	4.5
Teenagers	15.4	15.1	14.8	15.6	15.3	15.7	15.8
20-24 years old	8.2	8.3	7.7	7.7	7.8	7.3	8.0
Men, 25 years and older	3.5	3.3	3.6	3.5	3.5	3.5	3.4
Women, 25 years and older	3.7	3.5	3.5	3.5	3.5	3.6	3.6
<i>Labor force participation rate</i>							
Total	66.2	66.3	66.2	66.0	66.0	66.0	66.1
Teenagers	43.6	43.4	42.2	41.5	41.6	41.0	41.8
20-24 years old	74.6	75.0	75.1	74.2	74.3	73.8	74.5
Men, 25 years and older	75.5	75.7	75.7	75.6	75.6	75.6	75.5
Women, 25 years and older	59.6	59.8	59.6	59.6	59.4	59.6	59.7

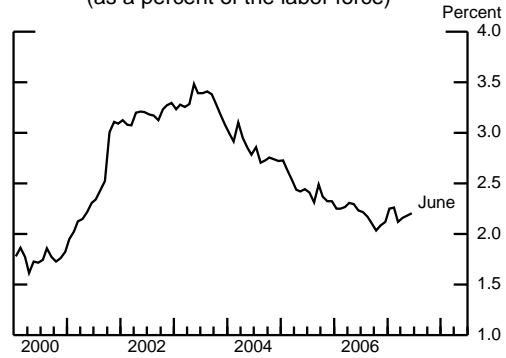
Labor Force Participation Rate and Unemployment Rate



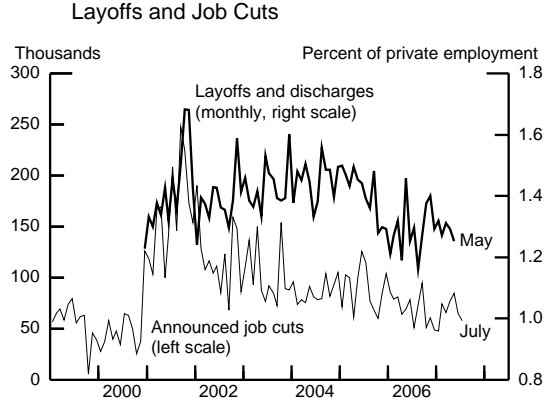
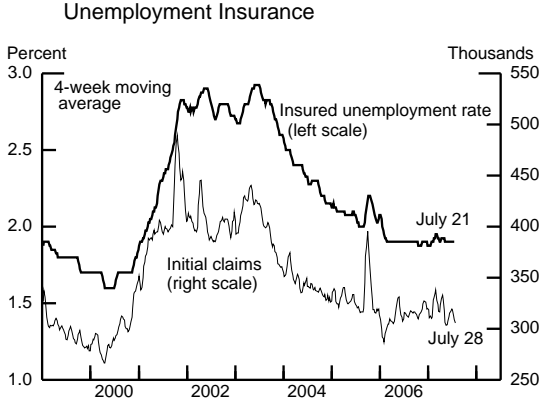
Job Losers Unemployed Less Than 5 Weeks
(as a percent of household employment)



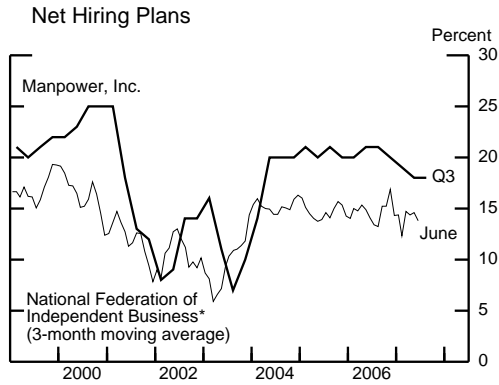
Unemployed Due to Job Loss
(as a percent of the labor force)



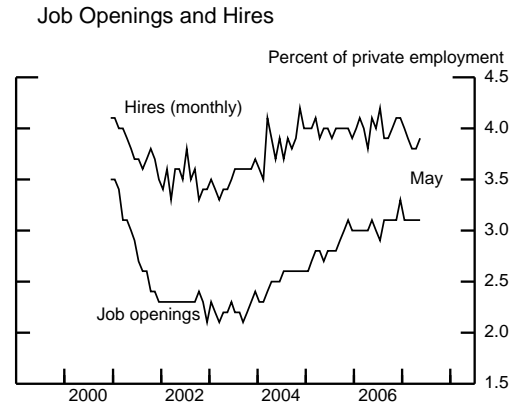
Labor Market Indicators



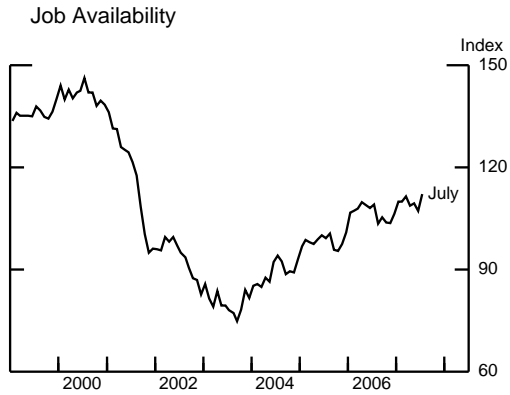
Note. Both series are seasonally adjusted by FRB staff.
Source. For layoffs and discharges, Job Openings and Labor Turnover Survey; for job cuts, Challenger, Gray, and Christmas, Inc.



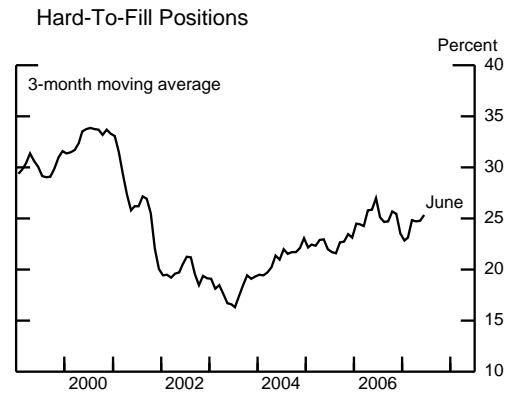
Note. Percent planning an increase in employment minus percent planning a reduction.
* Seasonally adjusted by FRB staff.



Source. Job Openings and Labor Turnover Survey.



Note. Proportion of households believing jobs are plentiful, minus the proportion believing jobs are hard to get, plus 100.
Source. Conference Board.



Note. Percent of small businesses surveyed with at least one "hard-to-fill" job opening. Seasonally adjusted by FRB staff.
Source. National Federation of Independent Business.

The staff estimates that productivity in the nonfarm business sector rose at an annual rate of 2 percent in the second quarter after a 0.7 percent rate of increase in the first quarter. The staff also estimates that over the past four quarters, productivity rose only 0.7 percent, 0.9 percentage point lower than the increase over the preceding four quarters.

Output per Hour

(Percent change from preceding period at an annual rate; seasonally adjusted)

Sector	2005:Q2 to 2006:Q2	2006:Q2 to 2007:Q2	2006		2007	
			Q3	Q4	Q1	Q2
Nonfarm business						
All persons	1.6	.7	-1.6	1.8	.7	2.0
All employees ¹	1.3	.7	-1.3	1.5	.3	2.4

Note. Staff estimates.

1. Assumes that the growth rate of hours of non-employees equals the growth rate of hours of employees.

Industrial Production

Industrial production (IP) increased at a moderate pace in the second quarter after little change, on net, over the previous two quarters. A smaller drag from inventory liquidation and a modest improvement in net trade appear to have been the primary contributors to IP growth in the second quarter after subtracting from growth in the previous quarter. Manufacturing IP appears poised to post solid gains in the near term, as days' supply of inventories are now at comfortable levels in most industries and indicators of activity, including the available weekly data for July, have shown continued strength.

Manufacturing production popped up 0.6 percent in June after no change in May; for the second quarter as a whole, output increased at an annual rate of nearly 3½ percent. The factory operating rate rose in June to 80.3 percent, slightly above its 1972–2006 average but below its recent peak last August.

After dropping for six consecutive quarters, the output of motor vehicles and parts jumped at an annual rate of 13.3 percent in the second quarter. Light vehicle assemblies rebounded from a very low first-quarter pace, while assemblies of medium and heavy trucks plunged further in the second quarter in the wake of new Environmental Protection

Selected Components of Industrial Production
(Percent change from preceding comparable period)

Component	Proportion 2006 (percent)	2006 ¹	2007		2007		
			Q1	Q2	Apr.	May	June
			Annual rate		Monthly rate		
Total	100.0	3.5	1.1	2.9	.4	-.1	.5
Previous	100.0	3.5	.8	...	.4	.0	...
Manufacturing	81.9	3.4	.8	3.4	.2	.0	.6
Ex. motor veh. and parts	76.3	3.9	1.4	2.7	.1	.0	.4
Ex. high-tech industries	71.5	2.5	.9	2.2	.0	.0	.4
Mining	8.6	8.0	-4.8	1.5	-.1	.3	.5
Utilities	9.6	.3	8.7	-.4	2.8	-1.6	.3
<i>Selected industries</i>							
Energy	20.5	4.0	4.8	-1.0	.4	-.1	.2
High technology	4.8	24.6	9.2	10.6	.9	.3	1.5
Computers	1.2	12.1	32.8	19.3	1.0	1.4	1.0
Communications equipment	1.1	14.8	27.7	5.9	-.5	-1.0	.9
Semiconductors ²	2.6	34.8	-6.9	8.5	1.6	.2	2.0
Motor vehicles and parts	5.5	-3.8	-7.5	13.3	1.4	-.5	2.5
<i>Total ex. selected industries</i>	69.1	2.4	.1	2.7	.3	-.1	.4
Consumer goods	20.9	1.8	1.0	.8	.2	-.4	.4
Durables	4.0	-1.9	-3.6	2.7	.6	.0	.6
Nondurables	16.9	2.7	2.1	.4	.2	-.5	.3
Business equipment	7.8	10.2	-3.3	3.9	.2	.1	-.3
Defense and space equipment	1.7	2.0	-2.2	-2.2	1.2	.5	.7
Construction supplies	4.5	-2.2	-3.0	3.5	.1	.3	1.0
Business supplies	7.9	1.0	.0	1.7	-.1	-.2	.3
Materials	26.1	2.3	1.1	4.2	.4	-.1	.6
Durables	14.5	2.0	1.3	6.4	.8	.3	.6
Nondurables	11.6	2.6	1.0	1.5	.0	-.6	.5

1. From fourth quarter of preceding year to fourth quarter of year shown.

2. Includes related electronic components.

... Not applicable.

Capacity Utilization
(Percent of capacity)

Sector	1972- 2006 average	1994- 95 high	2001- 02 low	2006	2007			
				Q4	Q1	Q2	May	June
Total industry	81.0	85.1	73.6	81.5	81.3	81.5	81.4	81.7
Manufacturing	79.8	84.6	71.6	80.1	79.8	80.1	79.9	80.3
Ex. motor veh. and parts	79.9	84.3	71.4	80.5	80.3	80.3	80.2	80.4
Mining	87.4	88.9	84.8	91.3	90.0	90.3	90.2	90.7
Utilities	86.7	93.7	83.8	85.0	86.4	86.0	85.4	85.6
<i>Stage-of-process groups</i>								
Crude	86.5	89.5	82.0	89.1	88.7	89.2	89.1	89.5
Primary and semifinished	82.2	88.2	74.6	82.3	82.2	82.2	82.0	82.4
Finished	77.8	80.5	70.0	78.2	78.0	78.3	78.1	78.3

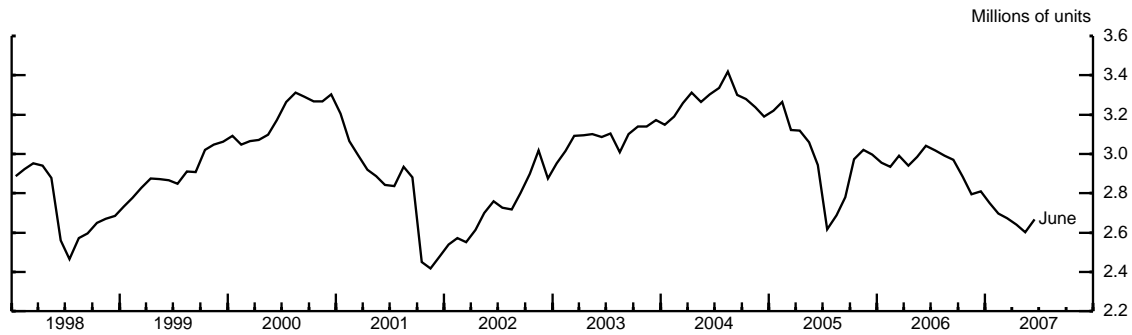
Production of Domestic Light Vehicles
(Millions of units at an annual rate except as noted)

Item	2006	2007			2007			
	Q4	Q1	Q2	Q3	June	July	Aug.	Sept.
U.S. production ¹	10.5	10.2	10.8	11.4	11.0	11.8	11.2	11.2
Autos	4.4	4.0	3.9	4.2	4.1	4.6	4.0	3.9
Light trucks	6.1	6.3	6.9	7.3	7.0	7.2	7.3	7.3
Days' supply ²	69	65	67	n.a.	69	n.a.	n.a.	n.a.
Autos	59	60	55	n.a.	56	n.a.	n.a.	n.a.
Light trucks	76	69	75	n.a.	80	n.a.	n.a.	n.a.
Inventories ³	2.81	2.67	2.67	n.a.	2.67	n.a.	n.a.	n.a.
Autos	1.02	1.00	.95	n.a.	.95	n.a.	n.a.	n.a.
Light trucks	1.79	1.67	1.72	n.a.	1.72	n.a.	n.a.	n.a.
Memo: U.S. production, total motor vehicles ⁴	11.0	10.6	11.1	11.8	11.3	12.1	11.6	11.5

Note. FRB seasonals. Components may not sum to totals because of rounding.

1. Production rates in the third quarter reflect the latest industry schedules.
 2. Quarterly values are calculated with end-of-period stocks and average reported sales.
 3. End-of-period stocks.
 4. Includes medium and heavy trucks.
- n.a. Not available.

Inventories of Light Vehicles

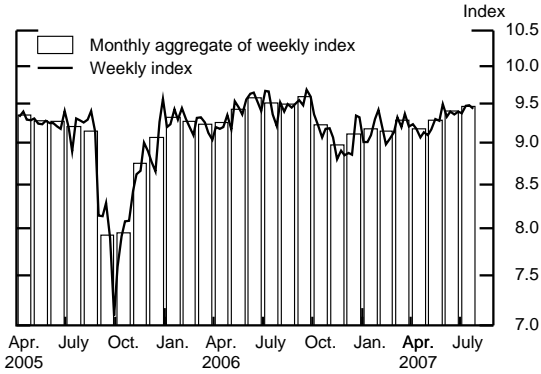


Days' Supply of Light Vehicles



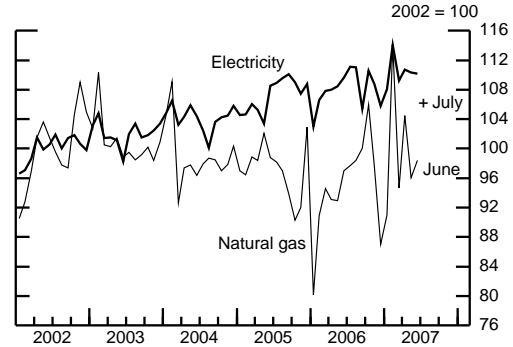
Indicators of Industrial Activity

Weekly Production Index excluding Motor Vehicles and Electricity Generation



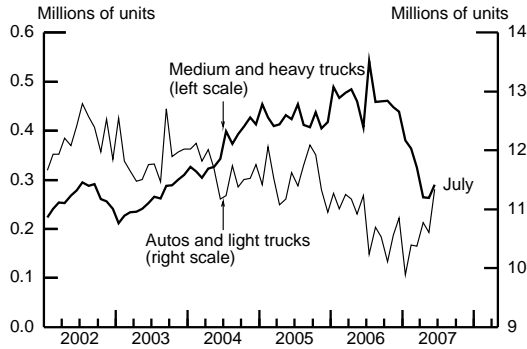
Note. One index point equals 1 percent of 2002 total industrial output.

Utilities Output



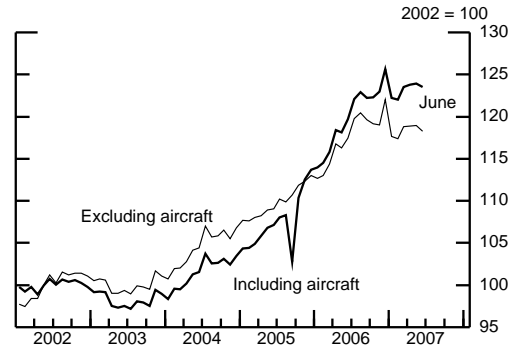
Note. July value for electricity generation is based on weekly data.

Motor Vehicle Assemblies

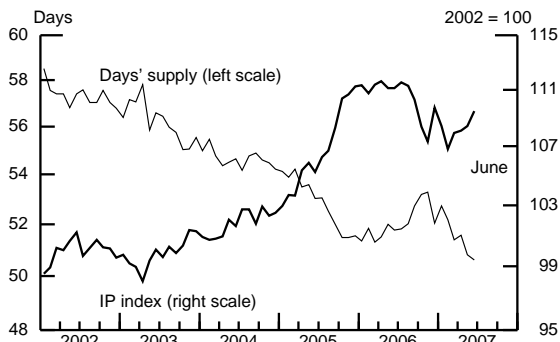


Note. July values are based on latest industry schedules.

Business Equipment IP Excluding High Tech and Motor Vehicles

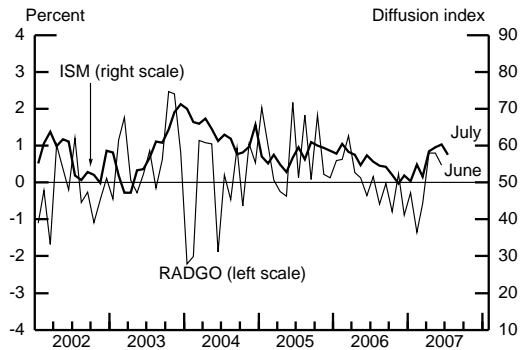


Construction Supplies



Note. Days' supply is from the staff's flow-of-goods system.

New Orders: ISM Survey and Change in Real Adjusted Durable Goods Orders (RADGO)



Note. The diffusion index equals the percentage of respondents reporting greater levels of new orders plus one-half the percentage of respondents reporting that new orders were unchanged. RADGO is a 3-month moving average.

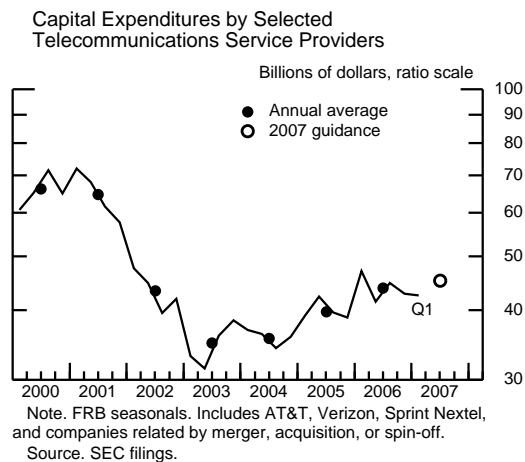
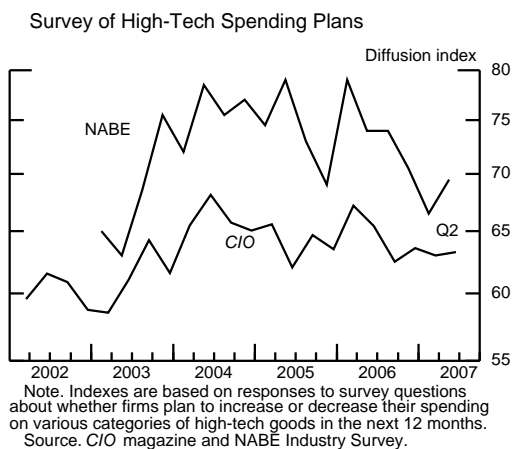
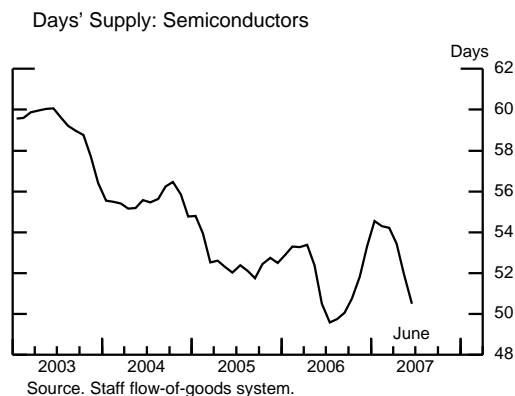
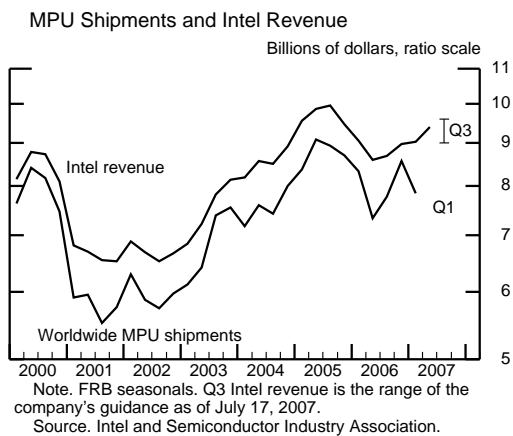
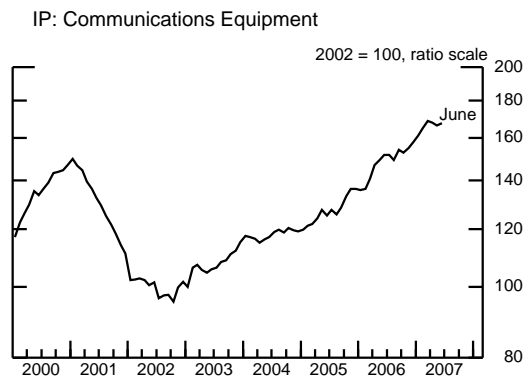
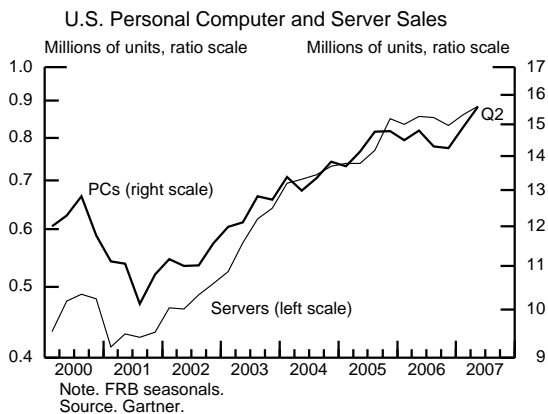
Agency (EPA) regulations on truck engines. With inventories of domestic light vehicles fairly well aligned with sales at the end of the second quarter, production schedules for the third quarter call for the pace of assemblies to step up again. However, these plans may prove too aggressive if demand does not pick up when the new 2008 model-year vehicles are introduced this fall.

Output in high-tech industries recorded another comparatively lackluster gain, on balance, in the second quarter. The output of computers decelerated to a more moderate pace after a first-quarter surge in production related to the retail release of Microsoft's new Vista operating system. Gains in production of communications equipment also slowed appreciably last quarter after stepping up sharply in the first quarter. The output of semiconductors, which fell at the beginning of the year, rose only modestly in the second quarter. Chip production was likely restrained by softer demand from downstream industries and by the manufacturers' efforts to reduce their bloated inventories. Stocks still appear somewhat elevated, and revenue guidance from Intel is consistent with only moderate increases in the output of microprocessors in the third quarter. Among other near-term indicators, National Association for Business Economics (NABE) and *CIO* magazine surveys of business plans for future spending on high-tech equipment improved somewhat in the second quarter.

Excluding energy, motor vehicles and parts, and high-tech products, output increased 0.4 percent in June and was up at an annual rate of 2.7 percent in the second quarter. After a series of declines, output of durable consumer goods rose at a 2.7 percent pace, boosted by a rebound in the production of appliances, furniture, carpeting goods, and home improvement products. The production of business equipment moved up moderately in the second quarter and was supported by continued strength in commercial aircraft production. The output of construction supplies rose at an annual rate of 3.5 percent in the second quarter after declining for three consecutive quarters; increases in the output of supplies typically associated with nonresidential construction appear to account for the second-quarter gain, while supplies associated with residential construction continued to move down. The output of industrial materials moved up at a steady pace, aided by a rebound in demand from downstream industries such as motor vehicles, other consumer durables, and nonresidential construction, as well as by the return of days' supply to its trend.

Indicators of near-term manufacturing activity point to continued production gains in the next few months. In particular, a three-month moving average of the staff's measure of

Indicators of High-Tech Manufacturing Activity



real adjusted durable goods orders increased in June. The new orders diffusion index from the Institute for Supply Management (ISM) and an average of the new orders indexes from the various regional surveys both declined in July after moving up in the second quarter, but their levels remained consistent with moderate increases in manufacturing output. Finally, the available weekly data for July show solid gains in production for light motor vehicles, steel products, and crude oil. The increase in total IP, however, appears to have been restrained by a decline in output at utilities.

Motor Vehicles

Demand for light motor vehicles has softened considerably in recent months. After maintaining a moderate annual rate of about 16.4 million units in the first five months of the year, sales in June and July averaged just 15.4 million units, their slowest two-month pace in almost two years.

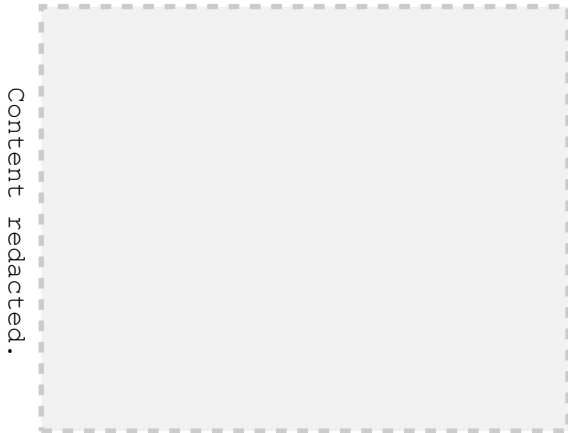
.¹ Consumers' anxiety about rising fuel prices and disappointment with the level of incentives being offered also appear to have played a role in restraining demand. So far this year, the sales decline has been concentrated in light trucks, a move that was felt primarily by domestic producers.

The near-term indicators of vehicle demand suggest that sales should improve a bit from their recent pace but remain tepid. Consumers' perceptions of car-buying conditions in the Reuters/University of Michigan survey recovered somewhat in July, although they remained at the low end of readings taken over the past year. The modest improvement in July mostly reflected a decline in the number of survey respondents who cited high gasoline prices as the reason that car-buying conditions were poor. Data from J.D. Power and Associates show that the average value of incentives for light vehicle purchases has changed little in recent months. At the end of July, however, General Motors introduced several new zero-percent financing programs in an effort to boost sagging demand, a move that in the past has induced similar programs at the other large firms.

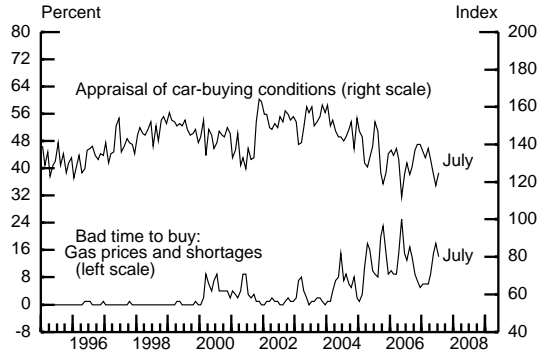
Sales of Light Vehicles
(Millions of units at an annual rate; FRB seasonals)

Category	2006	2006	2007				
		Q4	Q1	Q2	May	June	July
Total	16.5	16.3	16.4	16.0	16.3	15.6	15.2
Autos	7.8	7.6	7.6	7.7	8.0	7.6	7.2
Light trucks	8.7	8.7	8.9	8.4	8.2	8.0	8.0
North American ¹	12.8	12.5	12.6	12.3	12.5	11.9	11.6
Autos	5.4	5.2	5.1	5.3	5.5	5.2	4.9
Light trucks	7.4	7.2	7.4	7.0	6.9	6.6	6.7
Foreign-produced	3.7	3.8	3.9	3.8	3.8	3.8	3.6
Autos	2.3	2.4	2.4	2.4	2.5	2.4	2.3
Light trucks	1.3	1.4	1.4	1.4	1.3	1.4	1.3
Memo: Big Three domestic market share (percent) ²	53.7	52.3	52.1	51.8	51.8	50.1	48.3

Note. Components may not sum to totals because of rounding.
 1. Excludes some vehicles produced in Canada that are classified as imports by the industry.
 2. Domestic market share excludes sales of foreign brands affiliated with the Big Three.

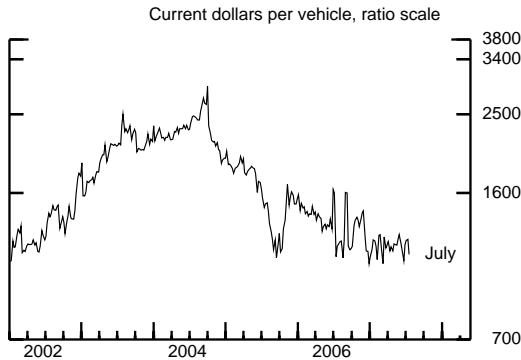


Car-Buying Attitudes



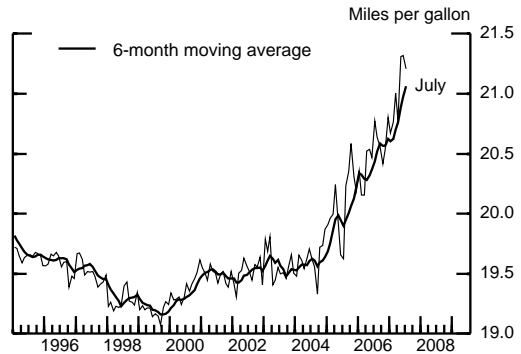
Source. Reuters/University of Michigan Survey.

Average Value of Incentives on Light Vehicles



Note. Weighted average of customer cash rebate and the present value of interest rate reduction. Data are seasonally adjusted.
 Source. J.D. Power and Associates.

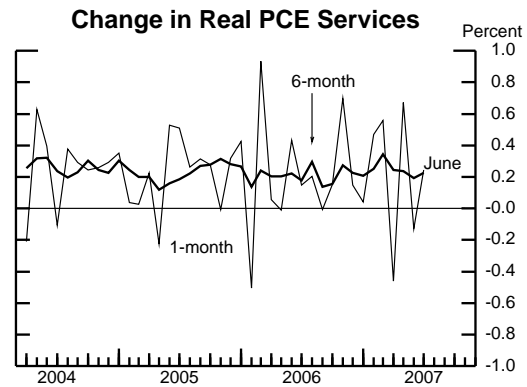
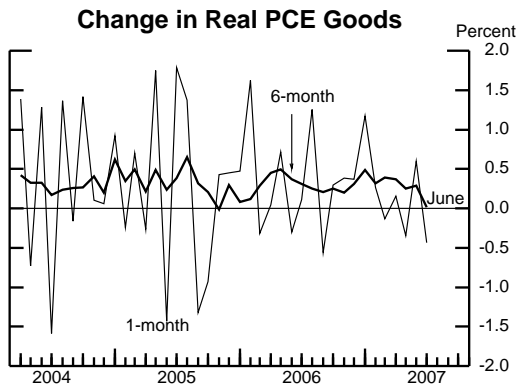
New Light Vehicle Fuel Economy



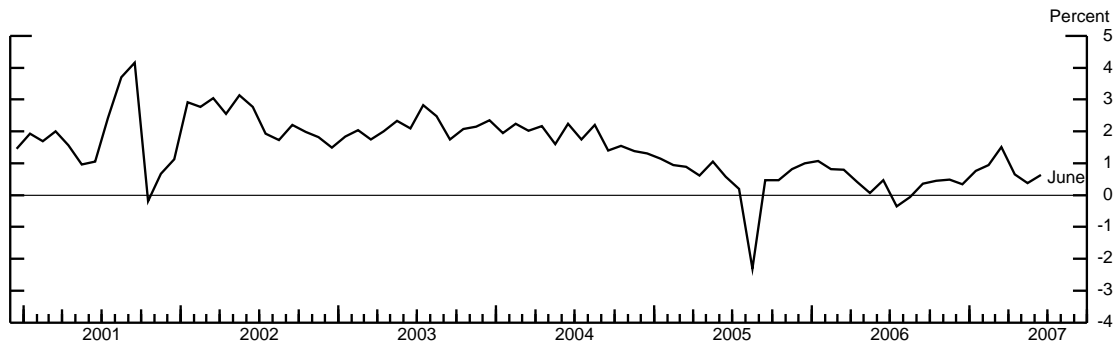
Source. Staff estimate based on a monthly sales-weighted average of city mileage ratings for all new models of light vehicles. Data are seasonally adjusted.

Real Personal Consumption Expenditures
(Percent change from the preceding period)

Category	2006		2007				
	2006	Q4	Q1	Q2	Apr.	May	June
	Annual rate			Monthly rate			
Total real PCE	3.1	3.9	3.7	1.3	.3	.2	.0
Durable goods	3.8	3.9	8.8	1.6	-.2	1.7	-1.6
Motor vehicles	-3.1	.1	11.3	-6	.1	1.6	-2.1
Excluding motor vehicles	9.1	6.6	7.1	3.3	-.4	1.8	-1.3
Nondurable goods	3.6	4.3	3.0	-.8	-.4	.2	.0
Energy	-.3	-5.6	2.4	-2.4	1.5	-1.6	.6
Other	4.2	5.8	3.1	-.6	-.7	.4	-.1
Services	2.7	3.7	3.1	2.2	.7	-.1	.2
Energy	-3.1	4.2	1.6	-4.9	17.2	-9.7	2.6
Other	2.9	3.7	3.2	2.5	.1	.3	.2
Memo: Real PCE goods ex. motor vehicles	4.5	4.9	4.0	-.1	-.4	.5	-.3



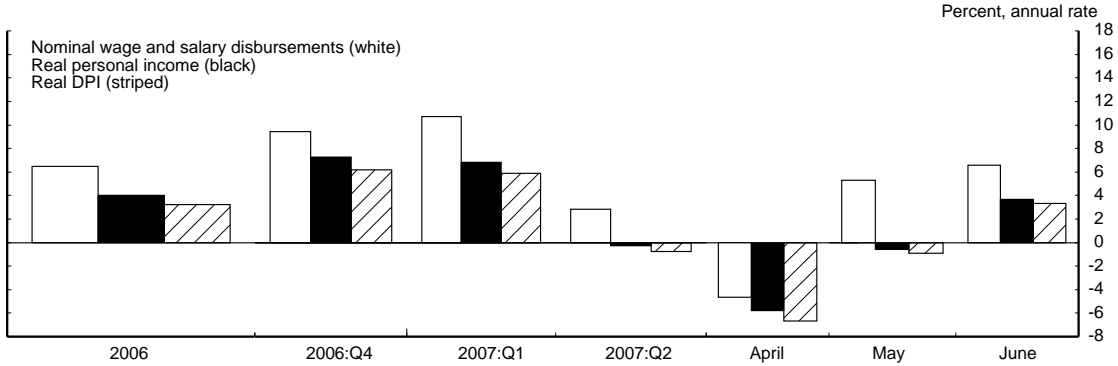
Personal Saving Rate



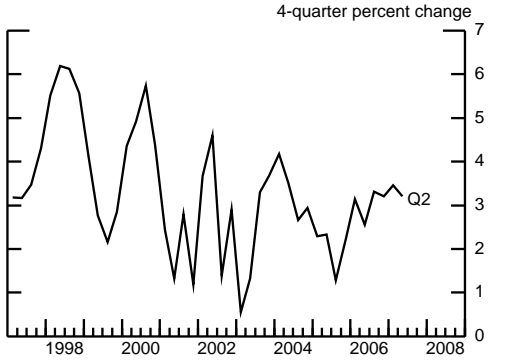
Note. Value for December 2004 excludes the effect on income of the one-time Microsoft dividend in that month.

Fundamentals of Household Spending

Changes in Nominal Wages and Salaries, Real Personal Income, and Real DPI

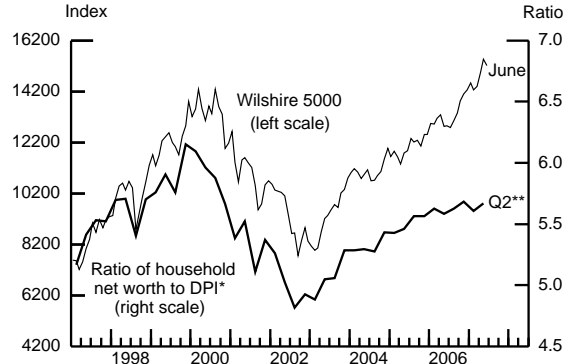


Change in Real DPI



Note. Values for 2004:Q4 and 2005:Q4 exclude the effect on income of the one-time Microsoft dividend in December 2004.

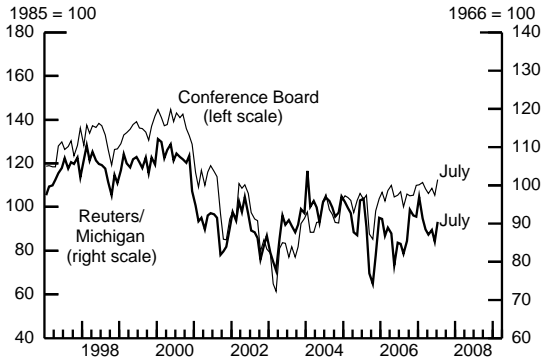
Household Net Worth and Wilshire 5000



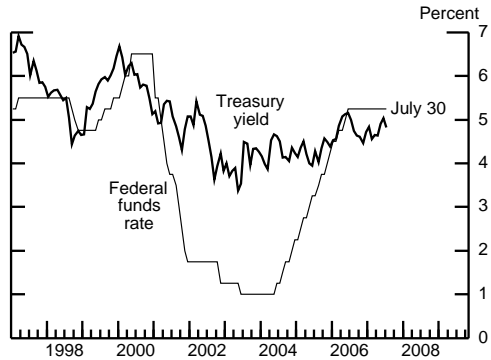
* The value for 2004:Q4 excludes the effect on income of the one-time Microsoft dividend in December 2004.

** Value for 2007:Q2 is a staff estimate.

Consumer Confidence



Federal Funds Rate and 10-Year Treasury Yield



Consumer Spending

The pace of consumer spending slowed considerably in the second quarter. The step-down came on the heels of a surge in purchases around the turn of the year, and at a time when a jump in energy prices was eroding the purchasing power of household income gains. Goods purchases, in particular, decelerated sharply as motor vehicle purchases dropped in the second quarter and real spending on other goods was subdued. Although increases in outlays on services slowed some last quarter as well, they are estimated to have continued advancing at a moderate pace.

Although the spike in energy prices damped real income growth in the second quarter, solid gains in wages and salaries and earlier increases in the stock market have generally been supportive of consumer expenditures. Real income growth was quite robust in the previous two quarters, and, despite the continued softness in house prices, household wealth moved markedly higher in the second quarter—mostly on the strength of the stock market, although equity prices have moved sharply lower more recently. Because the growth of outlays surpassed the change in disposable income in the second quarter, the personal saving rate fell to 0.6 percent.

Apart from sales of motor vehicles, other available indicators of spending in the third quarter are limited but seem to be a bit more upbeat. In particular, the latest readings on consumer sentiment and weekly data on chain store sales both point to a pickup in outlays early in the third quarter. In addition, weekly data on the volume of gasoline sales show an increase for July.

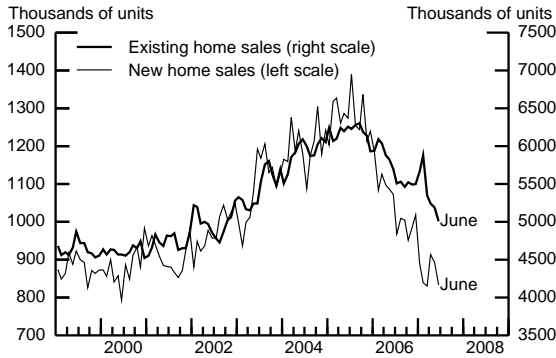
Housing

The housing sector remains very weak. Demand has been further restrained of late by higher interest rates—since mid-April, rates on thirty-year fixed-rate mortgages have risen about 50 basis points—and by increasingly tight lending standards in the subprime market. New home sales were down 11 percent and existing home sales down 6½ percent in the second quarter from their average levels in the second half of last year. With production flat despite the slower pace of demand, the inventory situation has shown little improvement, on balance, since the end of last year.

Most forward-looking indicators of housing demand—most notably, the index of pending home sales—have deteriorated, on balance, in the past few months. One exception is the four-week moving average of the mortgage purchase index, which has risen considerably,

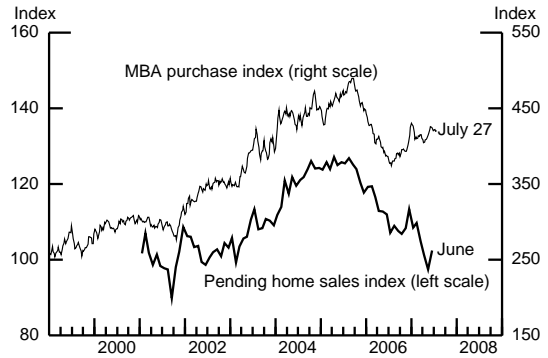
Indicators of Single-Family Housing

Home Sales



Source. For existing homes, National Association of Realtors; for new homes, Census Bureau.

Homebuying Indicators



Note. Purchase index is a 4-week moving average and is seasonally adjusted by FRB staff.
Source. For pending home sales, National Association of Realtors; for purchase index, Mortgage Bankers Assoc.

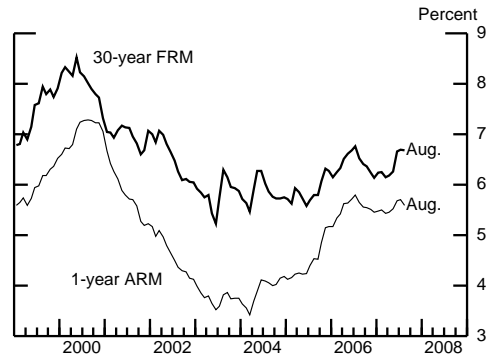
New Home Sales Months' Supply

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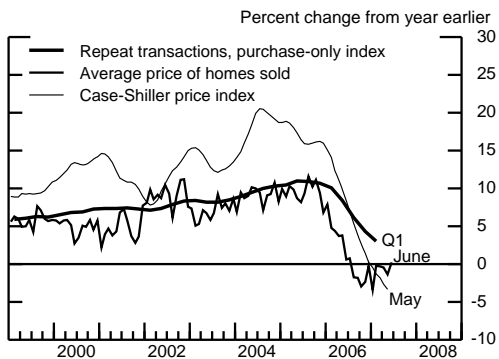
Note. Months' supply is calculated using the 3-month moving average of sales.
Source. ; for months' supply, Census Bureau.

Mortgage Rates



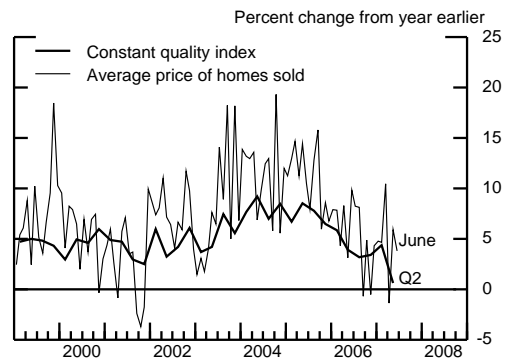
Note. The August readings are based on data through August 1, 2007.
Source. Freddie Mac.

Prices of Existing Homes



Note. The Case-Shiller price index is the 10-city index.
Source. For repeat transactions, OFHEO; for average price, National Association of Realtors; for Case-Shiller, Chicago Mercantile Exchange.

Prices of New Homes



Note. Average price values have been adjusted by Board staff to take into account new sampling procedures adopted in 2005.
Source. Census Bureau.

on net, since mid-April. However, the rise in this index may be somewhat misleading because of distortions related to the recent developments in subprime mortgage markets.²

Despite the apparent falloff in demand, new housing production has moved sideways this year. Single-family starts held steady in June at an annual rate of 1.15 million units. In contrast, adjusted permit issuance slipped further to an annual rate of 1.05 million units. Starts generally have tracked higher than permits since early 2006, and builders have evidently made up the shortfall by drawing down the sizable backlog of unused permits that had accumulated over the course of the housing boom. Historically, such gaps have led starts to adjust toward permits. Moreover, inventories of unsold new homes remain stubbornly elevated relative to sales—about 50 percent higher than the upper bound of the fairly tight range of months' supply values recorded between 1997 and 2005.³ All told, these indicators suggest that single-family construction will likely decline further in the coming months. Multifamily starts in June were at an annual rate of 316,000 units, in line with readings seen so far this year and at the low end of the relatively narrow range the values have occupied for the past ten years or so.

The latest readings on house prices have continued to show some deceleration. In the first quarter, the purchase-only version of the repeat price index for existing homes calculated by the Office of Federal Housing Enterprise Oversight (OFHEO) was 3 percent higher than its level a year earlier, a considerably smaller increase than the 10 percent appreciation posted over the preceding four-quarter period. The ten-city version of the Case-Shiller repeat-price index has decelerated even more noticeably and has shown negative year-over-year rates of change for every month this year through May.⁴ Estimates of the average price of existing homes sold—which are available on a more timely basis than the other measures but are not quality adjusted—showed the price

² Among other things, the mortgage purchase index does not sample applications taken by mortgage brokers, who issue the overwhelming majority of subprime loans. Therefore, the index may not adequately reflect the dramatic falloff in new credit to this portion of the market. In addition, the index measures mortgage *applications* rather than *approvals*; because mortgage lending standards have become tighter this year for many borrowers, a smaller proportion of mortgage applications are likely to have been approved, and some borrowers may have applied to a larger number of lenders for a given loan.

³

⁴ Unlike the OFHEO index, which captures only sales backed by conforming mortgage loans, the Case-Shiller index reflects all arms-length sales transactions in the included cities. The cities covered by the Case-Shiller index are Boston, Chicago, Denver, Las Vegas, Los Angeles, Miami, New York, San Diego, San Francisco, and Washington, DC.

Private Housing Activity

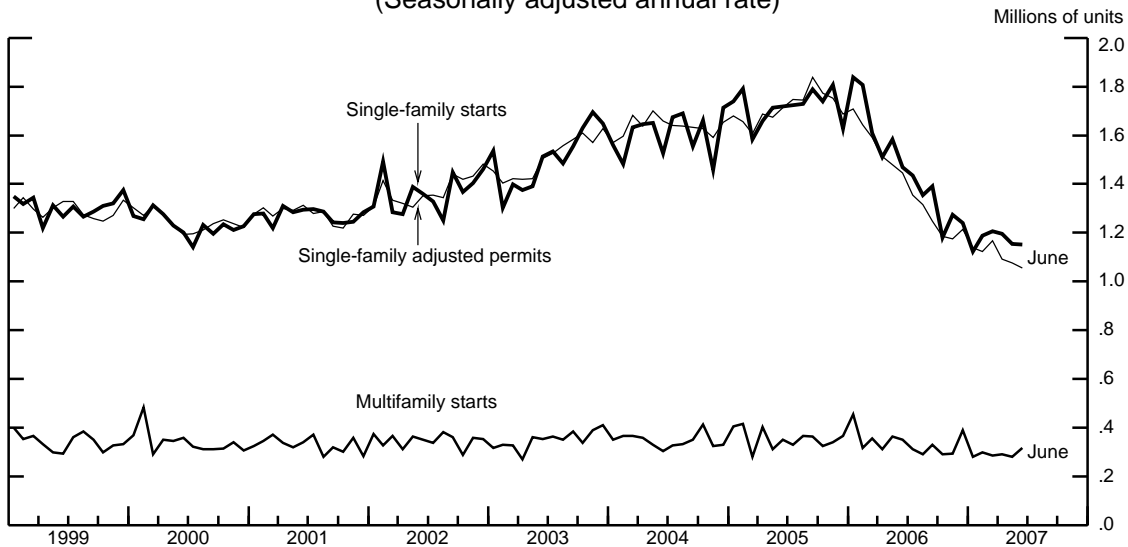
(Millions of units, seasonally adjusted; annual rate except as noted)

Sector	2006	2007				
		Q1	Q2	Apr.	May	June
<i>All units</i>						
Starts	1.80	1.46	1.46	1.49	1.43	1.47
Permits	1.84	1.56	1.46	1.46	1.52	1.41
<i>Single-family units</i>						
Starts	1.47	1.17	1.17	1.20	1.15	1.15
Permits	1.38	1.12	1.05	1.08	1.06	1.02
Adjusted permits ¹	1.41	1.14	1.07	1.09	1.08	1.05
Permit backlog ²	.134	.133	.117	.125	.127	.117
New homes						
Sales	1.05	.85	.88	.91	.89	.83
Months' supply ³	6.36	7.64	7.36	7.15	7.22	7.73
Existing homes						
Sales	5.68	5.63	5.15	5.24	5.19	5.01
Months' supply ³	6.36	7.08	8.25	8.02	8.44	8.30
<i>Multifamily units</i>						
Starts	.336	.288	.296	.290	.281	.316
Permits	.461	.440	.411	.382	.457	.394
Permit backlog ²	.062	.076	.080	.075	.082	.080
<i>Mobile homes</i>						
Shipments	.117	.094	n.a.	.097	.098	n.a.
<i>Condos and co-ops</i>						
Existing home sales	.801	.790	.767	.770	.790	.740

1. Adjusted permits equal permit issuance plus total starts outside of permit-issuing areas.
 2. Number outstanding at end of period. Excludes permits that have expired or have been canceled, abandoned, or revoked. Not at an annual rate.
 3. At current sales rate; expressed as the ratio of seasonally adjusted inventories to seasonally adjusted sales. Quarterly and annual figures are averages of monthly figures.
- n.a. Not available.

Private Housing Starts and Permits

(Seasonally adjusted annual rate)



Note. Adjusted permits equal permit issuance plus total starts outside of permit-issuing areas.

little changed in June relative to its level twelve months earlier. Similarly, the constant-quality price index for new homes—which adjusts for the geographic composition of sales, square footage, and other readily measurable attributes—was just 0.6 percent higher in the second quarter than four quarters earlier, down from the 3.9 percent appreciation posted in the preceding year.⁵ Although the quarterly data can be quite erratic, quality-adjusted prices fell at an annual rate of 9¼ percent during the second quarter—the first decline in this index during the current housing downturn.

Equipment and Software

Real business outlays for equipment and software (E&S) excluding transportation equipment posted a solid increase in the second quarter after having been flat, on net, in the preceding two quarters. Smoothing through the ups and downs, the recent pace has been modest and roughly consistent with the lackluster performance of the fundamental determinants of real E&S spending. Business output growth has stepped down somewhat since early last year, and while the user cost of high-tech capital has continued to decline, the trajectory is not particularly impressive by historical standards. Moreover, although firms retain ample cash in reserve to finance investment, credit costs for lower-grade borrowers have increased.

Real business outlays for high-tech E&S decelerated in the second quarter after a brisk first-quarter increase. Expenditures on computers and software rose at an annual rate of around 5½ percent last quarter after a very rapid Vista-influenced gain in the first quarter. Similarly, outlays on communications gear posted a solid 11 percent gain in the second quarter, on top of a much larger gain in the first quarter. However, guidance from telecommunications service providers suggests only modest growth in spending on communications equipment for 2007 as a whole.

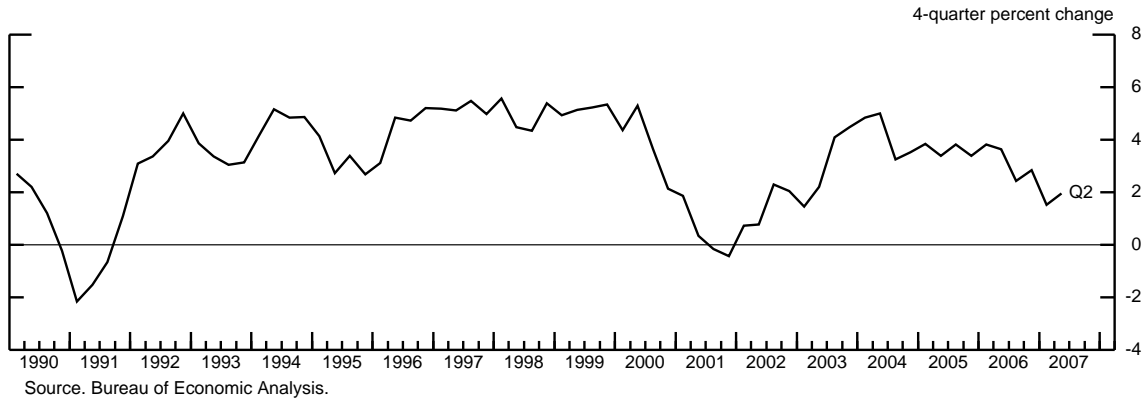
Business outlays on transportation equipment dropped at an annual rate of more than 28 percent in the second quarter, the third consecutive quarterly decline. Business-sector spending for motor vehicles fell,

. In addition to the payback from the large number of truck sales that were pulled into 2005 and 2006 ahead of the new EPA regulation on diesel engines, industry contacts also believe that part of the weakness in the sector is due

⁵ Even these quality-adjusted readings on new-home price appreciation may be overstated because builders reportedly have stepped up their use of nonprice incentives—such as granting more-favorable mortgage terms, paying closing costs, and including optional upgrades at no cost—over the past year to bolster sales and unload inventory.

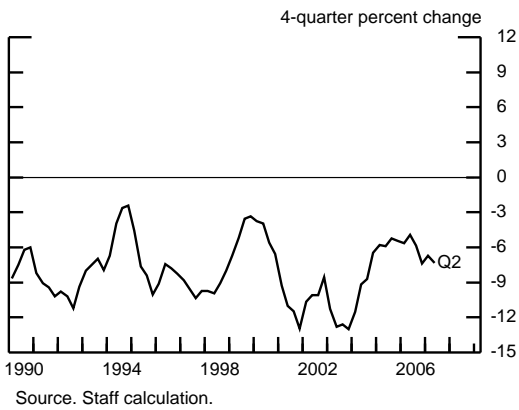
Fundamentals of Equipment and Software Investment

Real Business Output

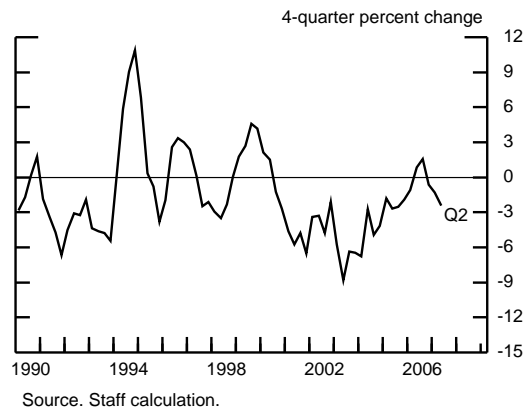


User Cost of Capital

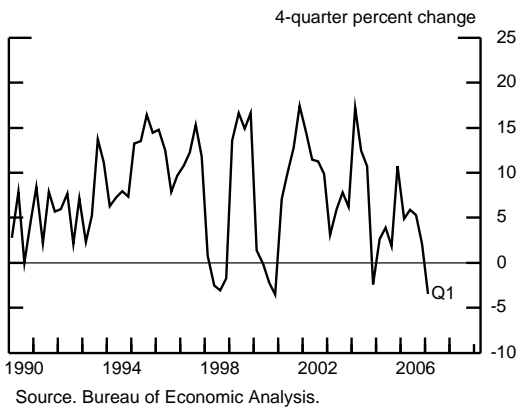
High-Tech



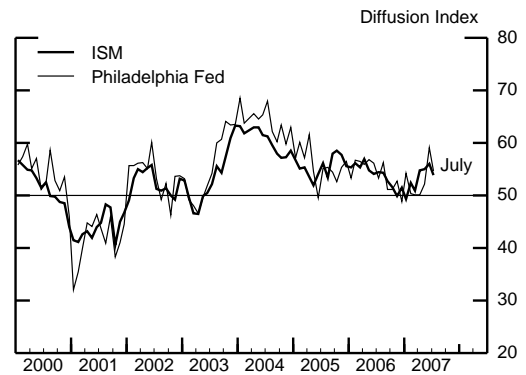
Non-High-Tech



Real Corporate Cash Flow



Surveys of Business Conditions



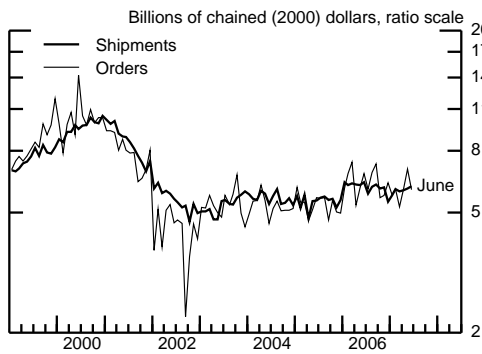
Orders and Shipments of Nondefense Capital Goods

(Percent change; seasonally adjusted current dollars)

Category	2007				
	Q1	Q2	Apr.	May	June
	Annual rate		Monthly rate		
Shipments	-8.8	10.8	1.1	.7	.3
Excluding aircraft	-11.1	10.7	.9	.7	-.1
Computers and peripherals	16.2	16.3	.7	12.5	-4.9
Communications equipment	2.4	13.9	1.4	1.0	1.7
All other categories	-14.7	9.8	.8	-.5	.3
Orders	-18.5	32.2	-.3	-6.8	5.2
Excluding aircraft	-16.2	13.3	2.0	-1.5	.0
Computers and peripherals	13.2	12.0	-6.3	15.3	-1.6
Communications equipment	-13.0	59.5	14.9	16.4	-14.8
All other categories	-19.0	9.7	1.8	-4.8	1.9
Memo: Shipments of complete aircraft ¹	46.2	n.a.	37.3	38.7	n.a.

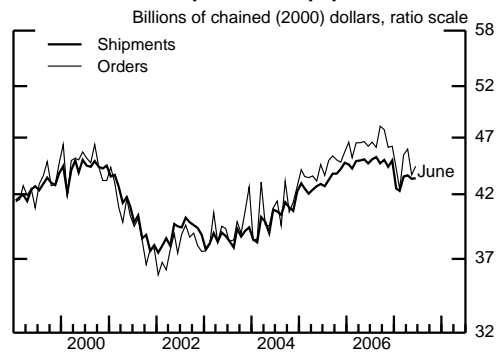
1. From Census Bureau, Current Industrial Reports; billions of dollars, annual rate.
n.a. Not available.

Communications Equipment



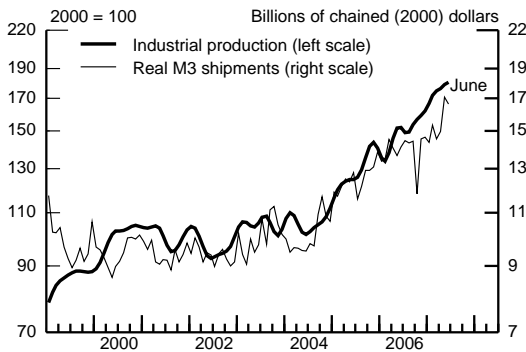
Note. Shipments and orders are deflated by a price index that is derived from the BEA's quality-adjusted price indexes and uses the PPI for communications equipment for monthly interpolation.

Non-High-Tech, Nontransportation Equipment



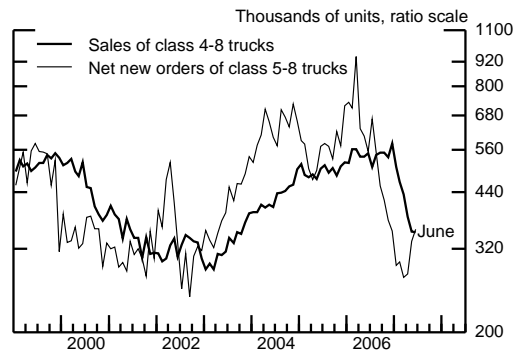
Note. Shipments and orders are deflated by the staff price indexes for the individual equipment types included in this category. Indexes are derived from the BEA's quality-adjusted price indexes.

Computers and Peripherals



Note. Ratio scales. Shipments are deflated by the staff price index for computers and peripheral equipment, which is derived from the BEA's quality-adjusted price indexes.

Medium and Heavy Trucks

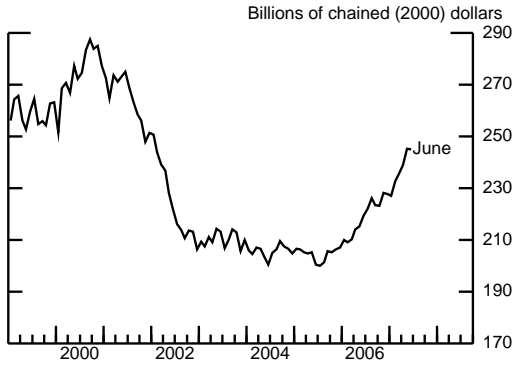


Note. Annual rate, FRB seasonals.
Source. For sales, Ward's Communications; for orders, ACT Research.

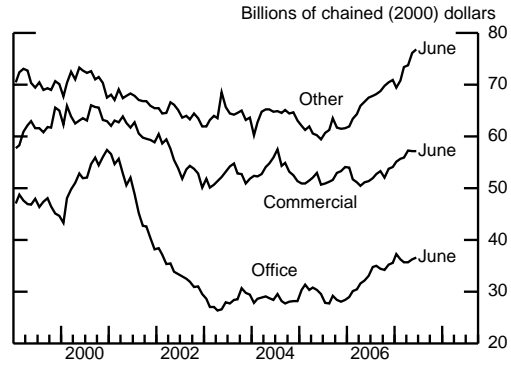
Nonresidential Construction and Indicators

(All spending series are seasonally adjusted at an annual rate; nominal CPIP deflated by BEA prices through Q1 and by staff projection thereafter)

Total Structures

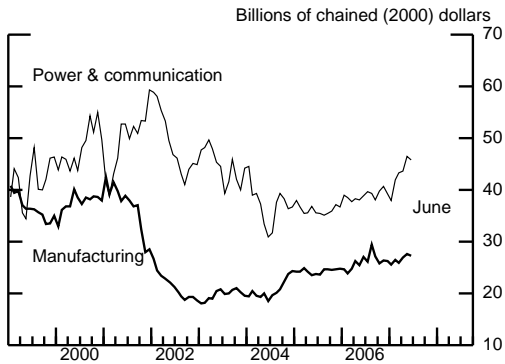


Office, Commercial, and Other

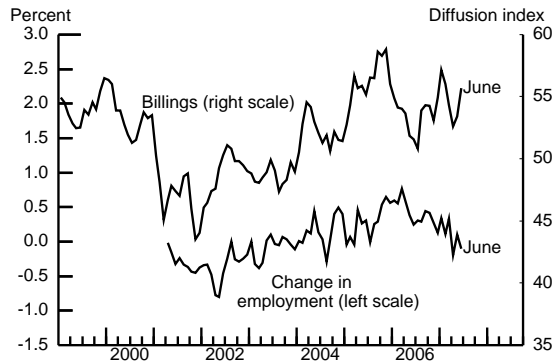


Note. Other includes religious, educational, lodging, amusement and recreation, transportation, and health-care facilities.

Manufacturing and Power & Communication

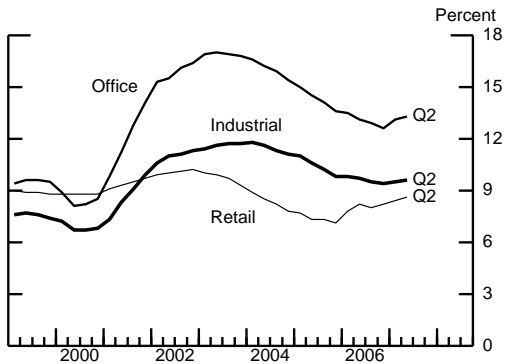


Architectural Billings and Nonresidential Construction Employment



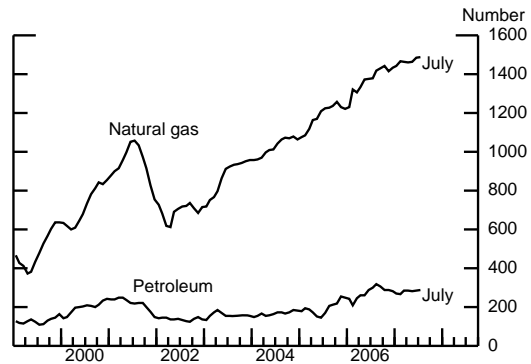
Note. Both series are 3-month moving averages. Employment includes industrial, commercial, and specialty trade construction. Source. For billings, American Institute of Architects; for employment, Bureau of Labor Statistics.

Vacancy Rates



Note. Industrial space includes both manufacturing structures and warehouses. Source. Torto Wheaton Research.

Drilling Rigs in Operation



Note. The July readings are based on data through July 27, 2007. Source. DOE/Baker Hughes.

to a slump in freight shipping volumes attributable to the slowdown in construction activity. New orders for medium and heavy trucks, meanwhile, edged up in the second quarter but remained at low levels. Domestic spending on aircraft spiked up in the first quarter from a very low level and stayed at that level in the second quarter.

Real spending on equipment other than high-tech and transportation surged at an annual rate of about 12 percent in the second quarter. The second-quarter increase recouped more than half of the steep decline in spending recorded over the prior three quarters, and the rebound was led by higher spending on industrial machinery. Outlays for mining, oil-field and gas-field equipment and for agricultural machinery also contributed to the second-quarter increase.

Looking ahead, surveys of business conditions, such as the ISM's monthly index and some regional indexes, have picked up considerably since earlier in the year and are consistent with solid growth in the near term. The most recent reading on the capital spending diffusion index derived from the NABE survey picked up as well. On the side of restraint, orders for nondefense capital goods excluding aircraft edged down in May and were flat in June.

Nonresidential Construction

Real spending on construction of nonresidential buildings has moved up smartly this year, and fundamentals in this sector remain solid. On the basis of available data, the staff estimates that spending on nonresidential structures excluding drilling and mining surged at an annual rate of more than 20 percent in the second quarter.⁶ In particular, vacancy rates, although up somewhat in recent quarters, are still relatively low by historical standards. Moreover, the three-month moving average of the diffusion index for architectural billings, which has some signal content for spending six months hence, points to continued gains in the coming quarters, albeit at a somewhat slower pace than seen so far this year.

According to the Bureau of Economic Analysis (BEA), activity in the drilling and mining segment jumped at an annual rate of 48 percent in the second quarter. This increase appears to be at odds with the data on the number of rigs in operation, which suggest that

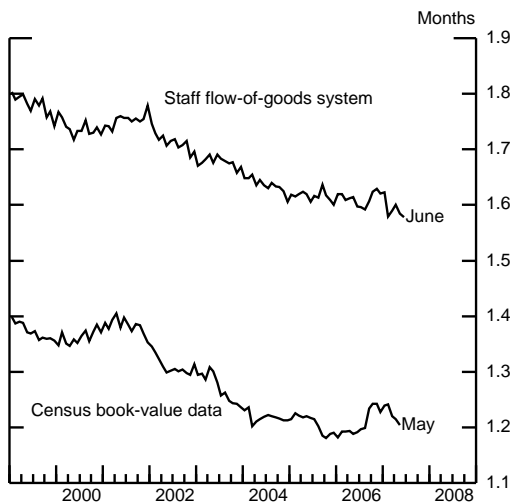
⁶ The June data on nonresidential construction was released after the BEA's advance GDP estimate for the second quarter. After incorporating the June data, we estimate that real nonresidential structures investment excluding drilling and mining grew 5.6 percentage points more than the BEA's advance second-quarter estimate.

Nonfarm Inventory Investment
(Billions of dollars; seasonally adjusted annual rate)

Measure and sector	2006	2007				
	Q4	Q1	Q2	Apr.	May	June
<i>Real inventory investment (chained 2000 dollars)</i>						
Total nonfarm business	13.6	-5.8	-.5^e	n.a.	n.a.	n.a.
Motor vehicles	-16.8	-14.7	-10.4 ^e	n.a.	n.a.	n.a.
Nonfarm ex. motor vehicles	30.4	8.9	9.9 ^e	n.a.	n.a.	n.a.
Manufacturing and trade ex. wholesale and retail motor vehicles and parts						
Manufacturing	-1.8	-5.0	n.a.	.6	-2.9^e	n.a.
Wholesale trade ex. motor vehicles & parts	5.3	4.3	n.a.	17.9	2.1	n.a.
Retail trade ex. motor vehicles & parts	11.3	1.8	n.a.	1.0	21.2	n.a.
<i>Book-value inventory investment (current dollars)</i>						
Manufacturing and trade ex. wholesale and retail motor vehicles and parts	39.4	33.9	n.a.	77.3	70.7	n.a.
Manufacturing	7.3	4.8	23.3	26.4	24.7	18.9
Wholesale trade ex. motor vehicles & parts	17.5	22.0	n.a.	35.0	16.6	n.a.
Retail trade ex. motor vehicles & parts	14.6	7.2	n.a.	15.8	29.4	n.a.

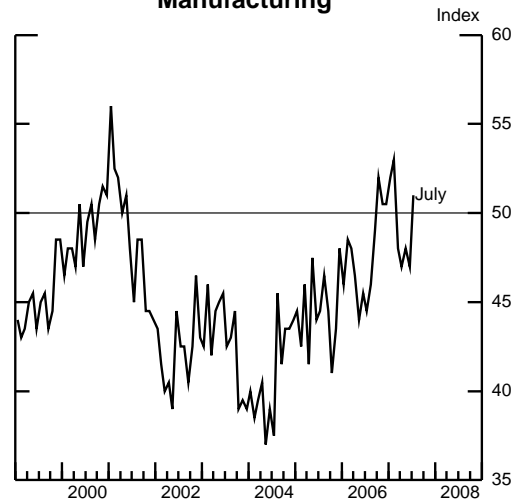
^e Staff estimate of real inventory investment based on revised book-value data.
n.a. Not available.
Source. For real inventory investment, BEA; for book-value data, Census Bureau.

Inventory Ratios ex. Motor Vehicles



Note. Flow-of-goods system covers total industry ex. motor vehicles and parts, and inventories are relative to consumption. Census data cover manufacturing and trade ex. motor vehicles and parts, and inventories are relative to sales.

ISM Customer Inventories: Manufacturing



Note. A number above 50 indicates inventories are "too high."

drilling activity has been flat, on balance, so far this year.⁷ Moreover, anecdotal reports in the most recent Beige Book suggest that incentives for further expansion of drilling for natural gas have been damped considerably by recent price declines and by persistently high inventories.

Business Inventories

Businesses have made considerable progress bringing inventories more into line with sales. We estimate that real nonfarm inventory investment excluding motor vehicles increased at an annual rate of \$9 billion in the second quarter, considerably below the pace in the second half of last year.⁸ Furthermore, the ratio of manufacturing and trade book-value inventories relative to sales, excluding motor vehicles, ticked down again in May. Similarly, the staff's flow-of-goods inventory system suggests that inventories in June were well aligned with absorption of final and intermediate goods. In July, the number of purchasing managers who viewed their customers' inventories as "too high" slightly exceeded the number who saw them as "too low."

Federal Government Sector

With receipts growing about in line with nominal income and increases in outlays slowing appreciably, the federal budget deficit has narrowed. Over the twelve months ending in June, the cumulative deficit (adjusted for payment-timing shifts and financial transactions) was \$173 billion, about 1¼ percent of nominal GDP and almost \$90 billion less than in the twelve months ending in June 2006.⁹

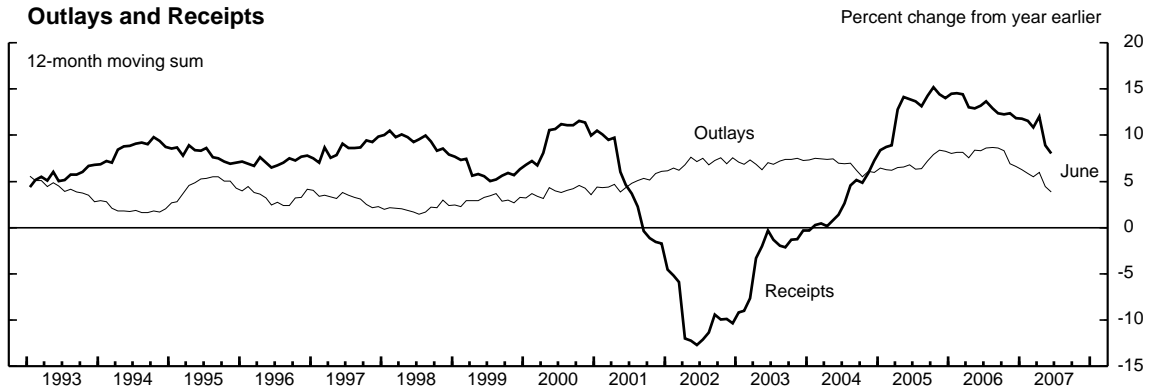
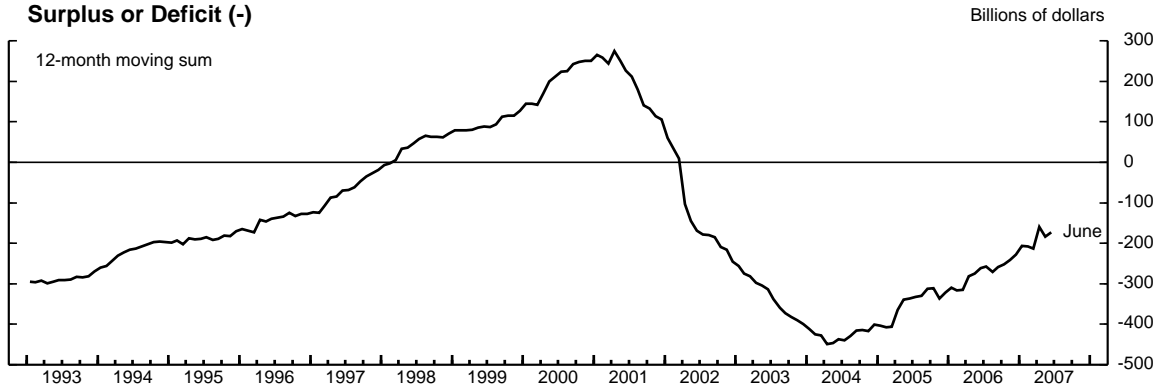
The growth of tax receipts has stepped down markedly of late from the exceptionally strong gains seen in recent years. In June, corporate revenues were only 2 percent higher than their level a year earlier, reflecting the slowing growth of profits. Individual income

⁷ To form their quarterly judgmental estimates of real spending growth in this category, the BEA extrapolates the quantity of drilling forward using proprietary data from the American Petroleum Institute (API) on footage drilled and estimated cost per foot, a second measure of footage drilled from the Department of Energy, and the number of drilling rigs in operation from Baker-Hughes. The proprietary data from the API receive about 60 percent of the weight in this calculation and are not available to the staff.

⁸ This estimate of inventory accumulation in the second quarter is \$1 billion higher than the advance estimate by the BEA for the quarter because it incorporates data for manufacturing inventories in June that were released after the BEA's estimate was calculated.

⁹ The Administration's *Mid-Session Review of the Budget* (MSR), which was released on July 11, projects the deficit for fiscal 2007 to be \$205 billion, narrower than the estimate of \$244 billion in the February budget but wider than suggested by the trend for the deficit over the first nine months of the fiscal year. Historically, the MSR has tended to be too pessimistic on the current-year deficit.

Federal Government Budget
 (Unified basis; adjusted for payment-timing shifts and financial transactions; data from Monthly Treasury Statement)



Recent Federal Outlays and Receipts

(Billions of dollars except as noted)

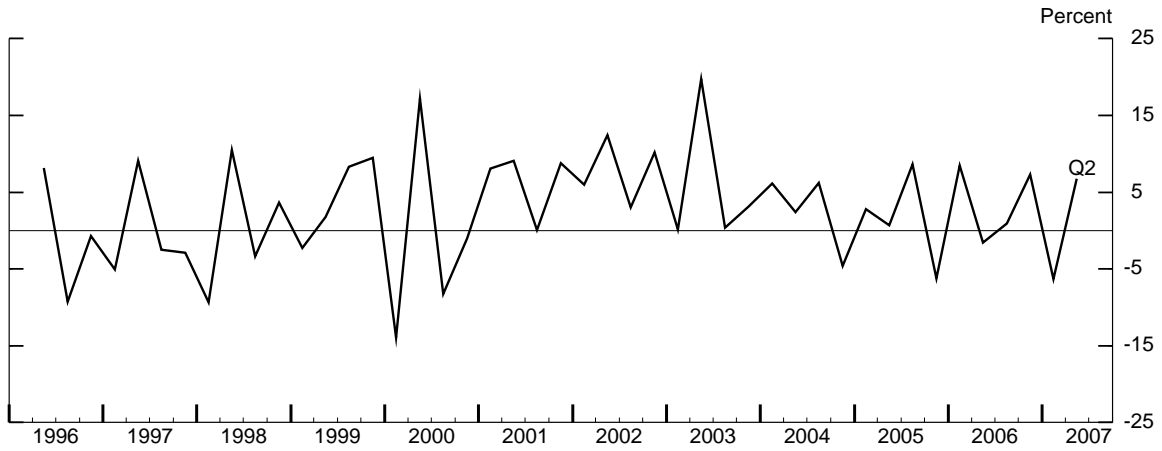
Function or source	June			12 months ending in June		
	2006	2007	Percent change	2006	2007	Percent change
Outlays						
Outlays	228.4	229.8	.6	2,620.8	2,721.6	3.8
Net interest	21.4	20.5	-4.2	212.3	234.4	10.4
National defense	47.2	48.7	3.2	518.8	551.4	6.3
Major transfers ¹	123.0	123.8	.7	1,405.4	1,496.4	6.5
Other	36.8	36.7	-.1	484.2	439.4	-9.3
Receipts						
Receipts	264.4	276.5	4.6	2,358.9	2,548.3	8.0
Individual income and payroll taxes	181.8	193.2	6.3	1,808.7	1,956.2	8.2
Corporate	67.3	68.6	2.0	331.6	382.3	15.3
Other	15.4	14.7	-4.5	218.6	209.8	-4.0
Surplus or deficit (-)	35.9	46.7	...	-261.9	-173.4	...

1. Includes Social Security, Medicare, Medicaid, and income security programs.

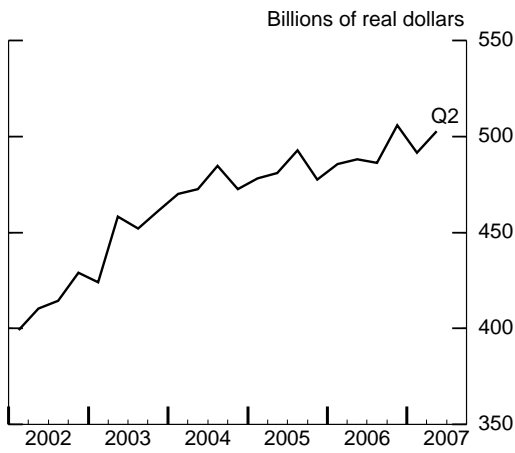
... Not applicable.

Federal Purchases in the National Income and Product Accounts
 (Billions of chained (2000) dollars, annual rate)

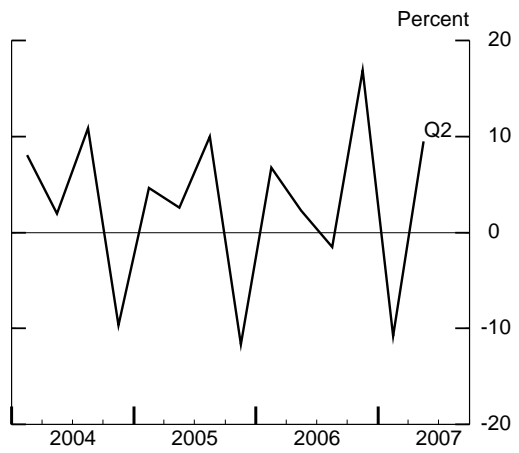
Total, Change



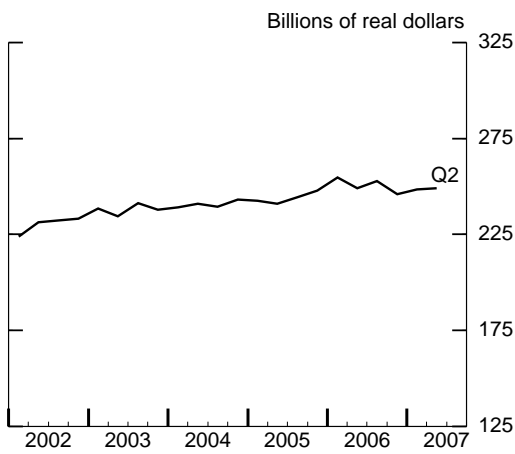
Defense, Level



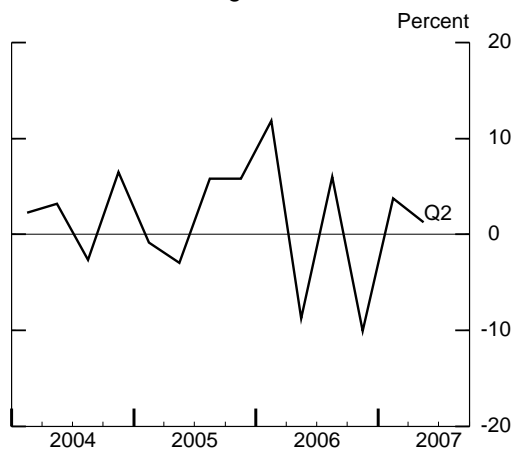
Defense, Change



Nondefense, Level

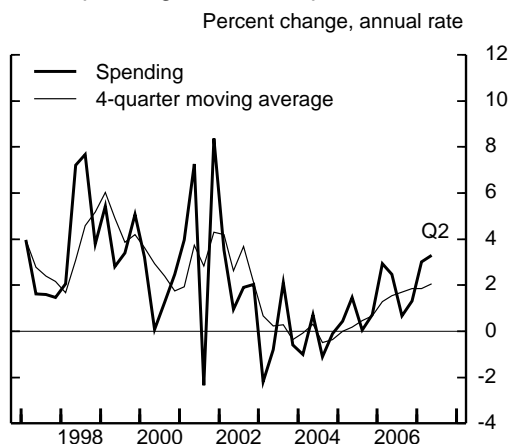


Nondefense, Change

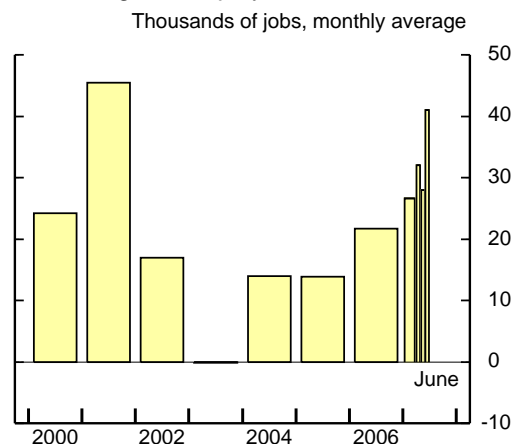


State and Local Indicators

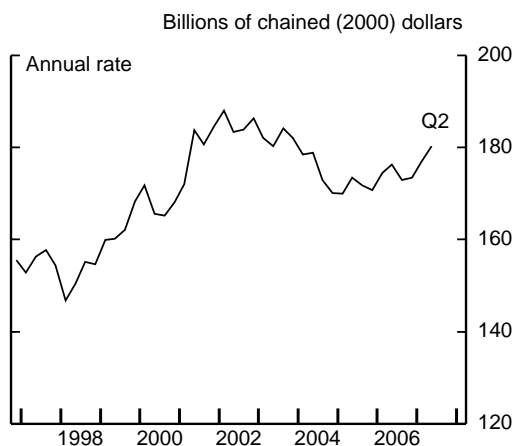
Real Spending on Consumption & Investment



Net Change in Employment

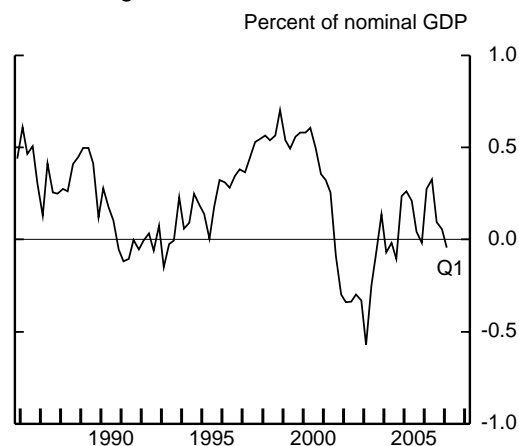


Real Construction

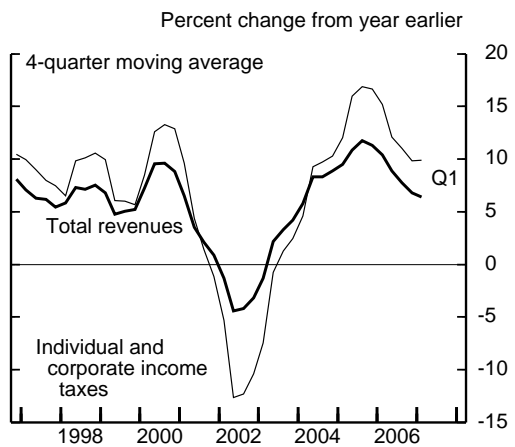


Note. Nominal CIPPI deflated by BEA prices.

Net Saving

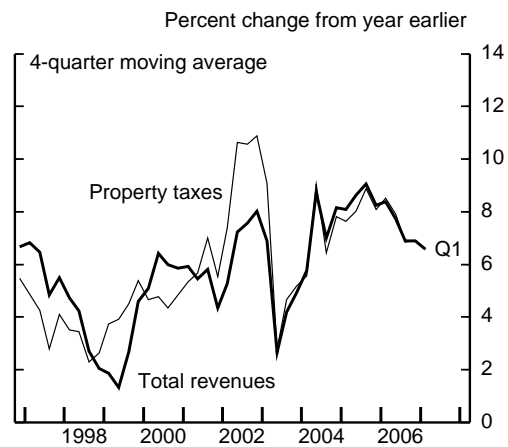


State Revenues



Source. Census Bureau.

Local Revenues



Source. Census Bureau.

and payroll tax payments in June were up 6¼ percent from their level a year earlier, compared with a 8¼ percent increase during the twelve months ending in June.

The deceleration in federal outlays was more pronounced than that in receipts. Total spending in June was barely above its level in June 2006. Spending for defense and the major transfer programs grew more slowly in June than their average monthly pace over the past year, and net interest payments in June declined a bit from their year-earlier level.

As measured in the national income and product accounts (NIPAs), total real federal purchases rose briskly in the second quarter and contributed nearly ½ percentage point to the rate of growth in real GDP. The rise in total federal purchases primarily reflected a bounceback in defense purchases; nondefense purchases edged up only a bit.

State and Local Government Sector

Healthy fiscal positions have contributed to solid increases in expenditures by state and local governments so far this year. State and local employment increased an average of 34,000 per month in the second quarter, significantly above the monthly average of 22,000 between 1997 and 2006. Construction expenditures have been climbing relatively rapidly for more than a year, and real investment in structures is estimated to have risen at a brisk annual rate of 7½ percent in the second quarter. Overall, the staff estimates that real purchases by state and local governments advanced at an annual rate of 3¼ percent in the second quarter.¹⁰

While state governments are believed to have ended the recent fiscal year in June with substantial cash reserves, revenues began slowing last year, and the Census Bureau's *Quarterly Summary of State and Local Tax Revenue* suggests that revenues continued to decelerate to a more moderate pace in the first quarter of 2007. In addition, recent anecdotal reports point to emerging concern by some state governments about their future fiscal positions. In particular, several large states, including California, Illinois, and Pennsylvania, have struggled to enact budgets for the current fiscal year, which began on July 1. Meanwhile, other states, including Maryland, are looking for ways to reduce expenditures below their planned levels in order to avert deficits in the near future.

¹⁰ The June data on state and local construction were released after the BEA's advance GDP estimate for the second quarter. We estimate that, after incorporating the June data, real state and local purchases grew 0.4 percentage point more than the BEA's advance second-quarter estimate.

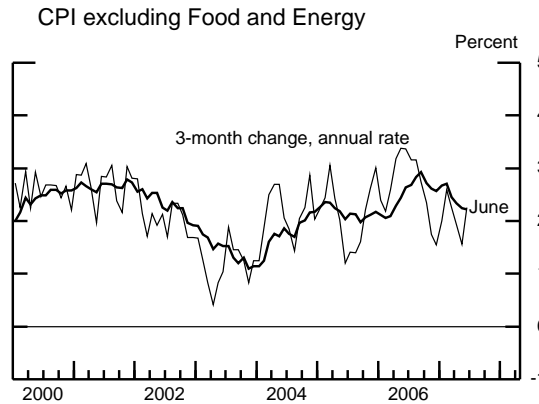
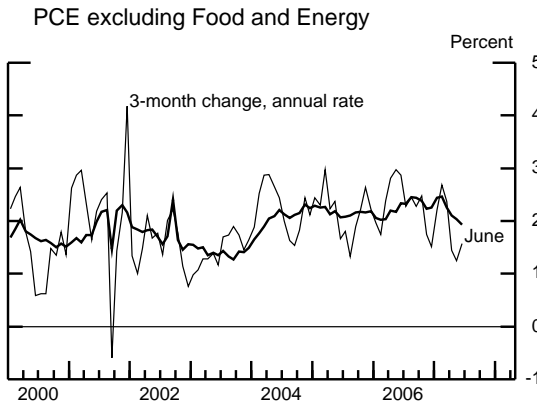
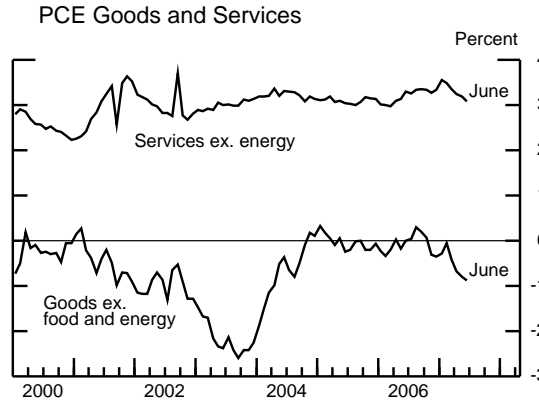
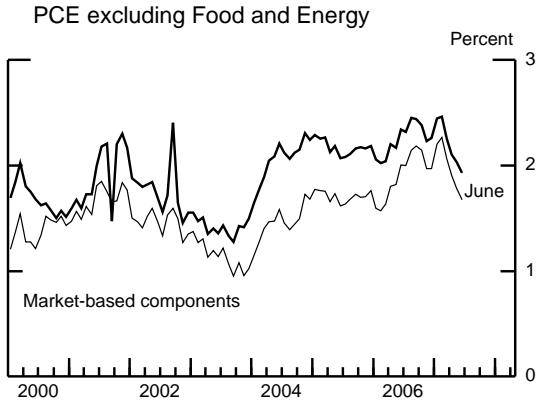
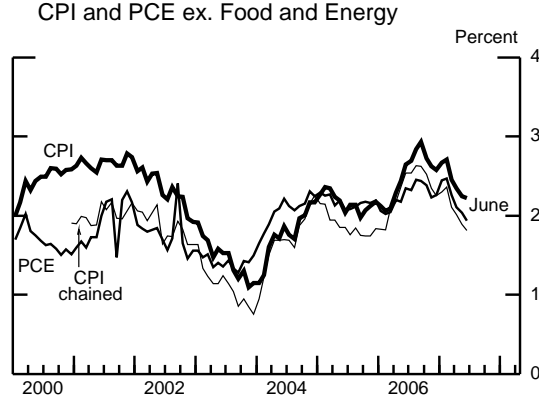
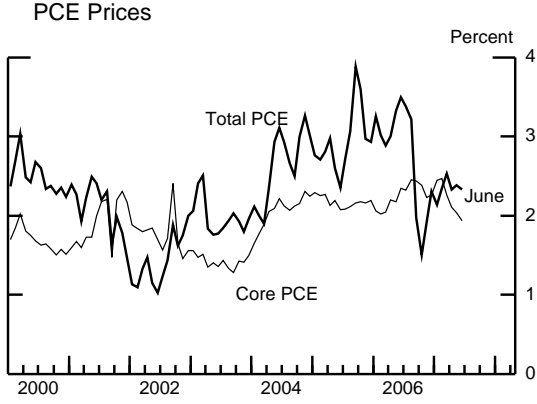
Price Measures
(Percent change)

Measures	12-month change		3-month change		1-month change	
	June 2006	June 2007	Annual rate		Monthly rate	
			Mar. 2007	June 2007	May 2007	June 2007
<i>CPI</i>						
Total	4.3	2.7	4.7	5.2	.7	.2
Food	2.2	4.1	7.3	5.1	.3	.5
Energy	23.3	4.6	22.9	32.9	5.4	-.5
Ex. food and energy	2.6	2.2	2.3	2.3	.1	.2
Core goods	.5	-.8	.4	-1.2	-.1	-.1
Core services	3.5	3.4	2.9	3.6	.3	.3
Shelter	3.5	3.8	2.5	4.1	.3	.4
Other services	3.4	2.8	3.2	3.2	.3	.3
Chained CPI (n.s.a.) ¹	3.8	2.3	...	...	...	...
Ex. food and energy ¹	2.5	1.8	...	...	...	...
<i>PCE prices</i>						
Total	3.5	2.3	4.1	3.8	.5	.1
Food and beverages	2.3	3.8	6.9	4.6	.3	.5
Energy	24.2	4.5	23.4	35.1	5.7	-.6
Ex. food and energy	2.3	1.9	2.4	1.6	.1	.1
Core goods	.0	-.9	.3	-1.8	-.2	-.2
Core services	3.3	3.1	3.2	2.9	.2	.3
Shelter	3.6	3.7	3.1	3.1	.2	.3
Other services	3.2	2.9	3.2	2.9	.3	.2
Core market-based	2.0	1.7	2.5	1.0	.1	.1
Core non-market-based	3.8	3.1	1.9	3.9	.4	.3
<i>PPI</i>						
Total finished goods	4.9	3.3	7.1	5.7	.9	-.2
Food	.4	6.5	19.3	-2.6	-.2	-.8
Energy	20.2	4.7	9.1	28.6	4.1	-1.1
Ex. food and energy	1.7	1.8	2.5	2.0	.2	.3
Core consumer goods	1.7	1.7	2.9	1.9	.3	.3
Capital equipment	1.7	1.8	2.2	1.6	.1	.3
Intermediate materials	9.5	3.7	5.7	10.4	1.1	.5
Ex. food and energy	7.4	2.8	2.4	6.6	.4	.4
Crude materials	8.7	14.8	36.0	3.3	2.0	.3
Ex. food and energy	35.2	10.2	58.3	1.1	.1	-.2

1. Higher-frequency figures are not applicable for data that are not seasonally adjusted.

... Not applicable.

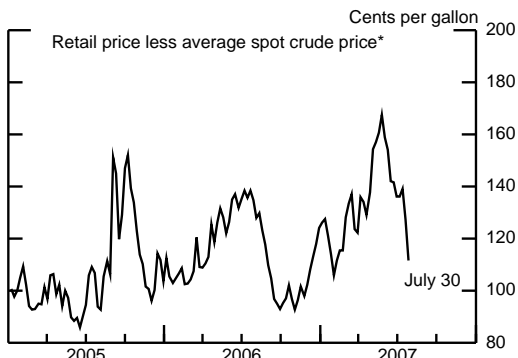
Consumer Prices (12-month change except as noted)



Energy Prices and Inventories

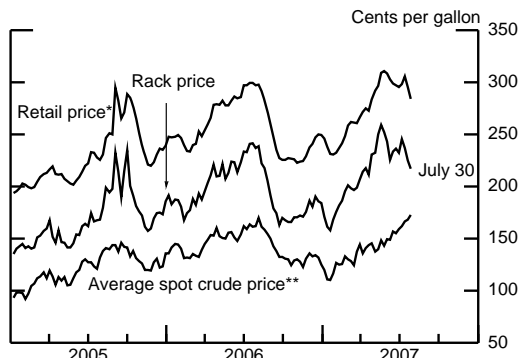
(Data from Energy Information Administration except as noted)

Total Gasoline Margin



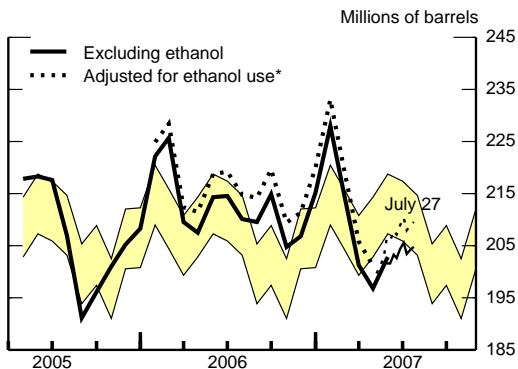
* Regular grade seasonally adjusted by FRB staff, less average spot crude price: 60% WTI, 40% Maya heavy crude.

Gasoline Price Decomposition



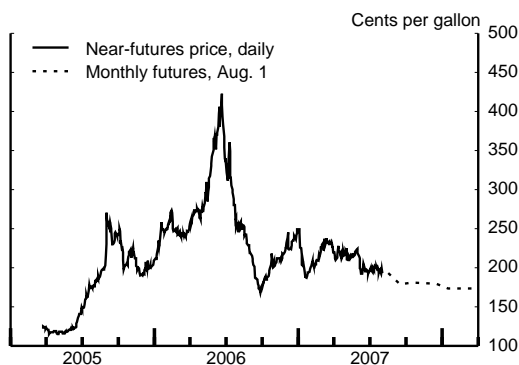
* Regular grade seasonally adjusted by FRB staff.
 ** 60% WTI, 40% Maya heavy crude.

Gasoline Inventories



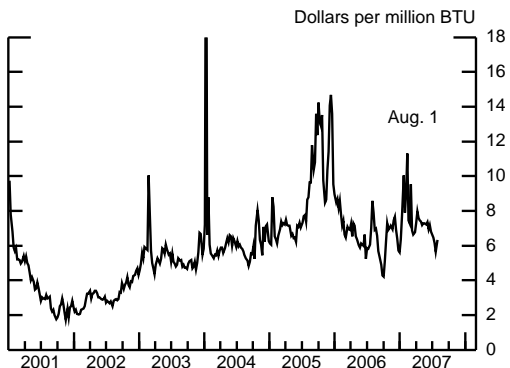
Note. Shaded region is average historical range as calculated by DOE. Monthly data through May 2007, weekly data thereafter, as indicated by line weights.
 * Adjustment for approximate amount of fuel ethanol to be blended with RBOB component of inventories; estimated by FRB staff.

Ethanol Prices



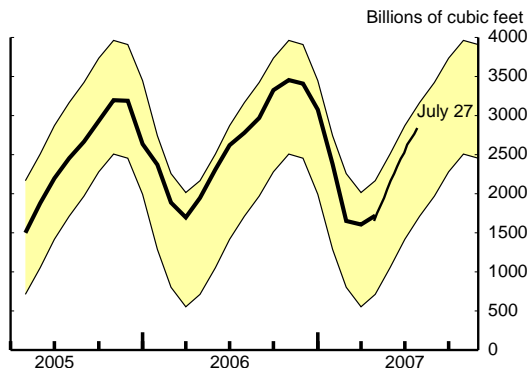
Source. Chicago Board of Trade.

Natural Gas Prices



Note. National average spot price.
 Source. Bloomberg.

Natural Gas Inventories



Note. Shaded region is defined as 5-year average plus seasonal factors +/- 1 standard deviation. Monthly data through April 2007, weekly data thereafter, as indicated by line weights.

Prices

Headline consumer price inflation slowed in June as energy prices flattened out after having increased rapidly over the preceding three months. Despite June's favorable outcome, total PCE prices were up at an annual rate of about 4 percent over the first half of this year, compared with 2¼ percent over the twelve months of 2006. Outside of food and energy, however, core inflation slowed in the first half of this year from last year's upward revised pace. Resource utilization still appears to be relatively tight, but long-run inflation expectations have remained within the range that has prevailed during much of the past few years.

Excluding food and energy, PCE prices rose 0.1 percent in June. Prices of core goods fell 0.2 percent, bringing the decrease in the first six months of this year to an annual rate of ¾ percent, a faster rate of decline than occurred in 2006. After rising modestly last year, apparel prices fell sharply in the first half of this year and more than accounted for the overall deceleration in core goods prices. Prices of core services rose 0.3 percent in June and were boosted by higher prices of housing services, particularly lodging away from home, which posted a sizable increase for the third consecutive month. Over the first half of this year, prices of core services rose at an annual rate of about 3 percent. This pace was ¼ percentage point lower than its rate in 2006, reflecting a sizable deceleration in owners' equivalent rent.

Energy prices declined 0.6 percent in June after a rise of 15 percent (not at an annual rate) over the previous three months. This substantial run-up in energy prices followed very large declines late last year; on balance, energy prices were up 4½ percent over the twelve months ending in June after rising more than 24 percent during the comparable period twelve months earlier. Gasoline prices fell 1 percent in June and appear to have declined again in July despite marked increases in crude oil input costs over the same period. Increased production at gasoline refineries has boosted inventories, and gasoline margins, while still elevated, have fallen well below their recent peak in May.

Food prices posted another large increase in June and continued to show signs of the pass-through of high corn prices, which have been boosted by strong demand for ethanol. In the first half of this year, the PCE price index for food and beverages has increased at an annual rate of 5¾ percent, a sizable step-up from the 2 percent increase in 2006. While this pickup has been widespread, price increases for meats, poultry, eggs, and dairy, for which corn is the main feedstuff, have been particularly large this year. That said, recent rains and USDA reports predicting a bumper harvest have pushed corn prices

Broad Measures of Inflation
(Percent change, Q2 to Q2)

Measure	2004	2005	2006	2007
<i>Product prices</i>				
GDP price index	2.9	3.0	3.5	2.7
Less food and energy	2.7	3.1	3.3	2.5
Nonfarm business chain price index	2.2	3.2	3.5	2.0
<i>Expenditure prices</i>				
Gross domestic purchases price index	3.1	3.4	3.8	2.6
Less food and energy	2.7	3.0	3.1	2.4
PCE price index	2.8	2.6	3.3	2.3
Less food and energy	2.1	2.1	2.2	2.0
PCE price index, market-based components	2.4	2.4	3.2	2.2
Less food and energy	1.5	1.7	1.9	1.8
CPI	2.8	2.9	4.0	2.7
Less food and energy	1.8	2.2	2.4	2.3
Chained CPI	2.7	2.6	3.4	2.3
Less food and energy	1.7	1.9	2.4	1.9
Median CPI	2.4	2.3	2.9	3.2
Trimmed mean CPI	2.1	2.2	2.7	2.7
Trimmed mean PCE	2.3	2.3	2.7	2.5

Surveys of Inflation Expectations
(Percent)

Period	Actual CPI inflation ¹	Reuters/Michigan Survey				Professional forecasters (10 years) ⁴
		1 year ²		5 to 10 years ³		
		Mean	Median	Mean	Median	
2005:Q3	3.8	4.3	3.5	3.5	2.9	2.5
Q4	3.7	4.6	3.7	3.5	3.1	2.5
2006:Q1	3.6	3.7	3.0	3.3	2.9	2.5
Q2	4.0	4.5	3.5	3.6	3.1	2.5
Q3	3.3	4.0	3.4	3.3	3.0	2.5
Q4	1.9	3.5	3.0	3.5	3.0	2.5
2007:Q1	2.4	3.6	3.0	3.4	2.9	2.4
Q2	2.7	4.2	3.3	3.5	3.0	2.4
Mar.	2.8	3.6	3.0	3.3	2.9	...
Apr.	2.6	4.0	3.3	3.6	3.1	...
May	2.7	4.3	3.3	3.7	3.1	2.4
June	2.7	4.2	3.4	3.3	2.9	...
July	n.a.	4.2	3.4	3.6	3.1	...

1. Percent change from the same period in the preceding year.

2. Responses to the question, By about what percent do you expect prices to go up, on average, during the next 12 months?

3. Responses to the question, By about what percent per year do you expect prices to go up, on average, during the next 5 to 10 years?

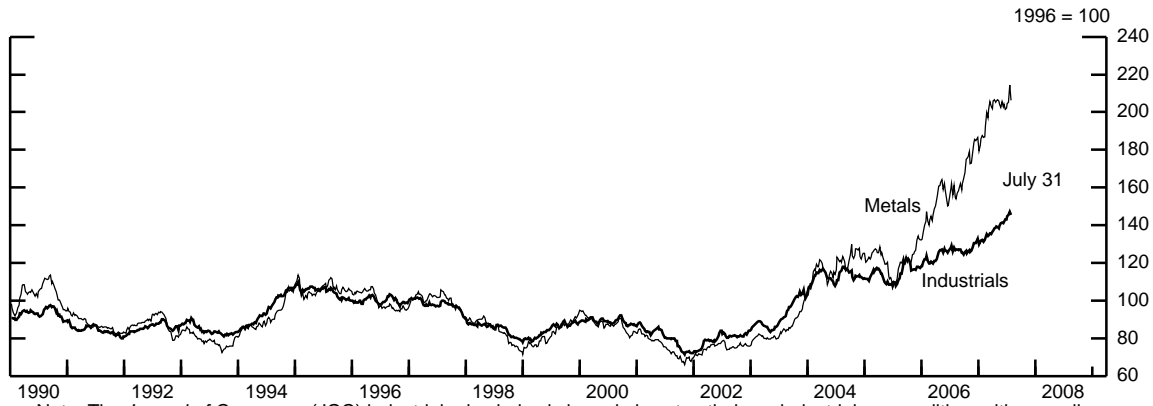
4. Quarterly CPI projections compiled by the Federal Reserve Bank of Philadelphia.

... Not applicable.

n.a. Not available.

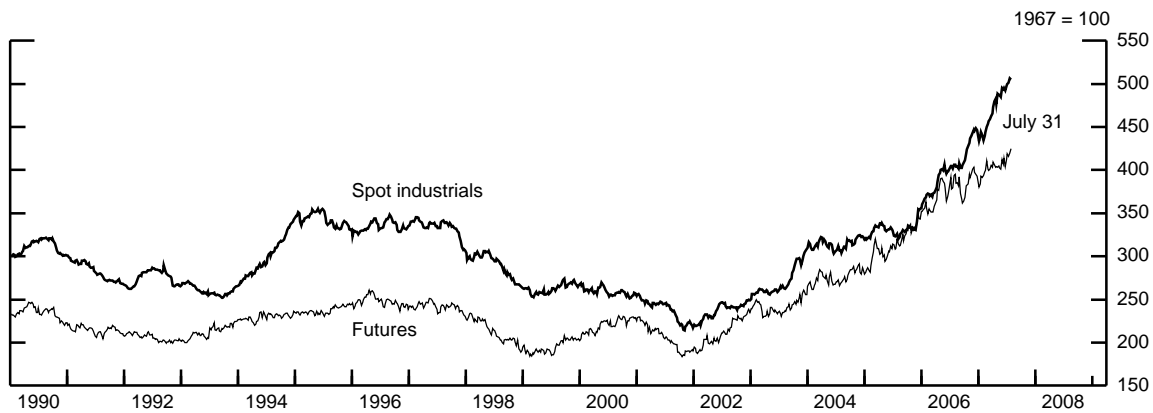
Commodity Price Indexes

Journal of Commerce



Note. The *Journal of Commerce* (JOC) industrial price index is based almost entirely on industrial commodities, with a small weight given to energy commodities. Copyright for *Journal of Commerce* data is held by CIBCR, 1994.

Commodity Research Bureau



Note. The Commodity Research Bureau (CRB) spot industrials index consists entirely of industrial commodities, excluding energy. The CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities, and precious metals.

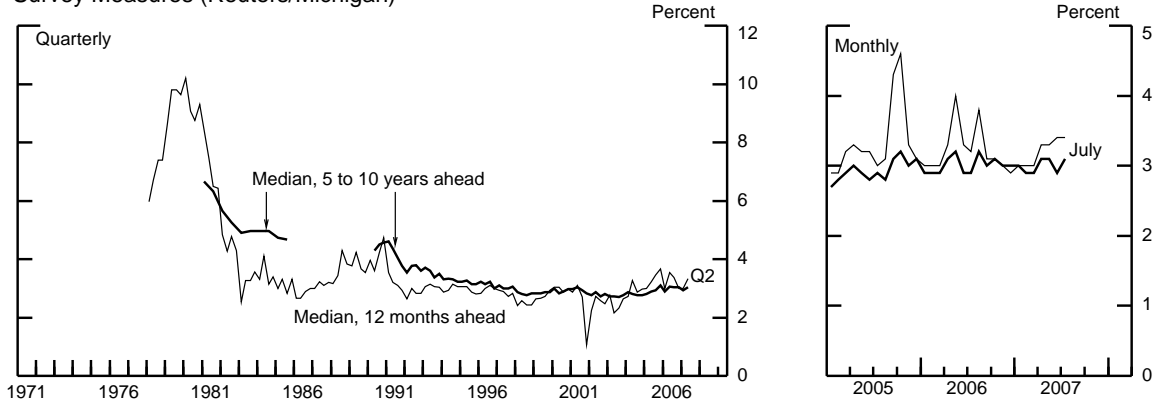
Selected Commodity Price Indexes (Percent change)

Index	2006 ¹	12/19/06 to 6/19/07 ²	6/19/07 ² to 7/31/07	52-week change to 7/31/07
JOC industrials	11.0	8.6	2.7	13.6
JOC metals	38.9	10.5	1.0	28.0
CRB spot industrials	26.9	10.5	2.0	24.3
CRB spot foodstuffs	13.0	20.2	-.7	23.6
CRB futures	15.0	4.6	2.6	7.8

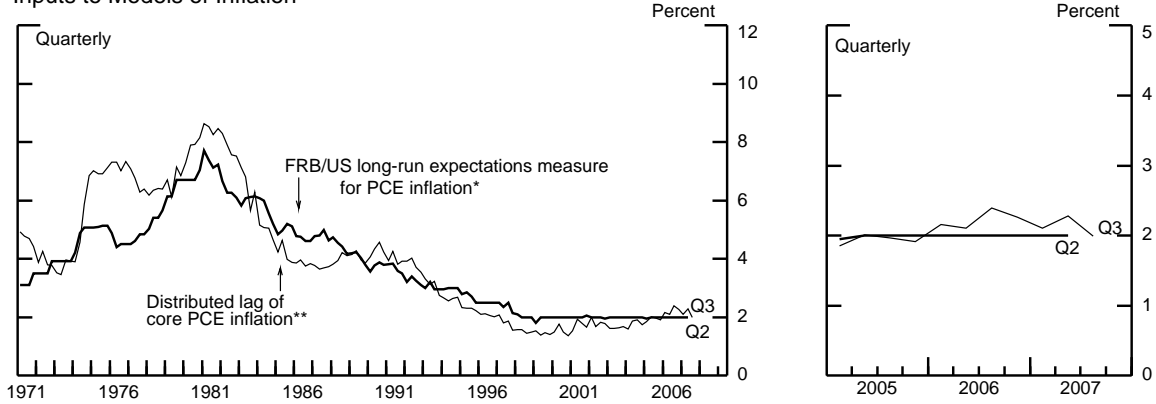
1. From the last week of the preceding year to the last week of the year indicated.
2. June 19, 2007, is the Tuesday preceding publication of the June Greenbook.

Measures of Expected Inflation

Survey Measures (Reuters/Michigan)

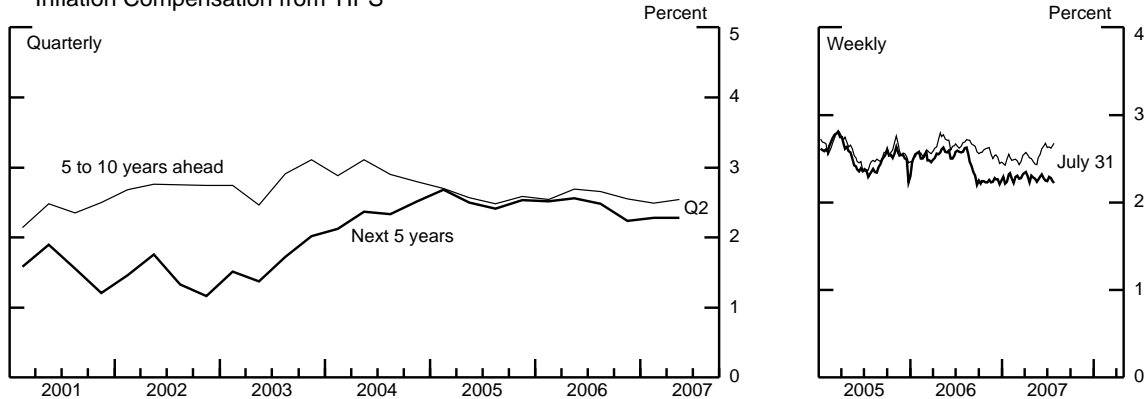


Inputs to Models of Inflation



*For 2007 forward, the median projection for PCE inflation over the next 10 years from the Survey of Professional Forecasters (SPF); for 1991 to 2006, the equivalent SPF projection for the CPI; for 1981 to 1991, a related survey for the CPI conducted by Richard Hoey; and for the period preceding 1981, a model-based estimate constructed by Board staff. The survey data before 2007 are adjusted down 0.5 percentage point to put the CPI projections approximately on a PCE basis.
 **Derived from one of the reduced-form Phillips curves used by Board staff.

Inflation Compensation from TIPS



Note. Based on a comparison of an estimated TIPS yield curve with an estimated nominal off-the-run Treasury yield curve, with an adjustment for the indexation-lag effect.

down considerably in recent weeks. Spot prices for slaughter-ready cattle, for which corn is the major feed source, have also dropped below their recent highs, and spot prices for poultry have merely flattened out in recent weeks.

Broader measures of inflation have slowed relative to the pace of the past few years. In the second quarter, the four-quarter change in the GDP price index was 2.7 percent, down $\frac{3}{4}$ percentage point from the increase over the preceding four-quarter period. GDP prices excluding food and energy have decelerated by a similar amount over this period. This slowdown reflects both a small deceleration in core PCE prices over this period and a considerable step-down in price increases for construction.

As measured by the Reuters/Michigan survey, the median expectation for year-ahead inflation increased to 3.4 percent in June and remained at that rate in July despite declines in gasoline prices in both months. The median expectation for inflation over the next five to ten years moved back up to 3.1 percent, near the top of the narrow range that has prevailed over the past few years. Inflation compensation from TIPS five-to-ten years ahead has changed little since the last FOMC meeting and remains at about its average level over the past couple of years.

Strong global demand and rising energy prices have continued to push up the prices of goods at earlier stages of processing this year. These prices have some, albeit small, predictive content for finished goods prices. The PPI for core intermediate materials increased 0.4 percent in both May and June and rose at an annual rate of $4\frac{1}{2}$ percent in the first half of this year, about the same as the pace over 2005 and 2006. Commodity prices have continued to move higher since the June Greenbook and are up considerably from their levels a year earlier. The *Journal of Commerce* index of industrial materials has risen about $2\frac{3}{4}$ percent since the June Greenbook, boosted in part by its energy components, and the Commodity Research Bureau's index of industrial spot prices, which includes excludes energy, was up 2 percent over the same period.

Labor Costs

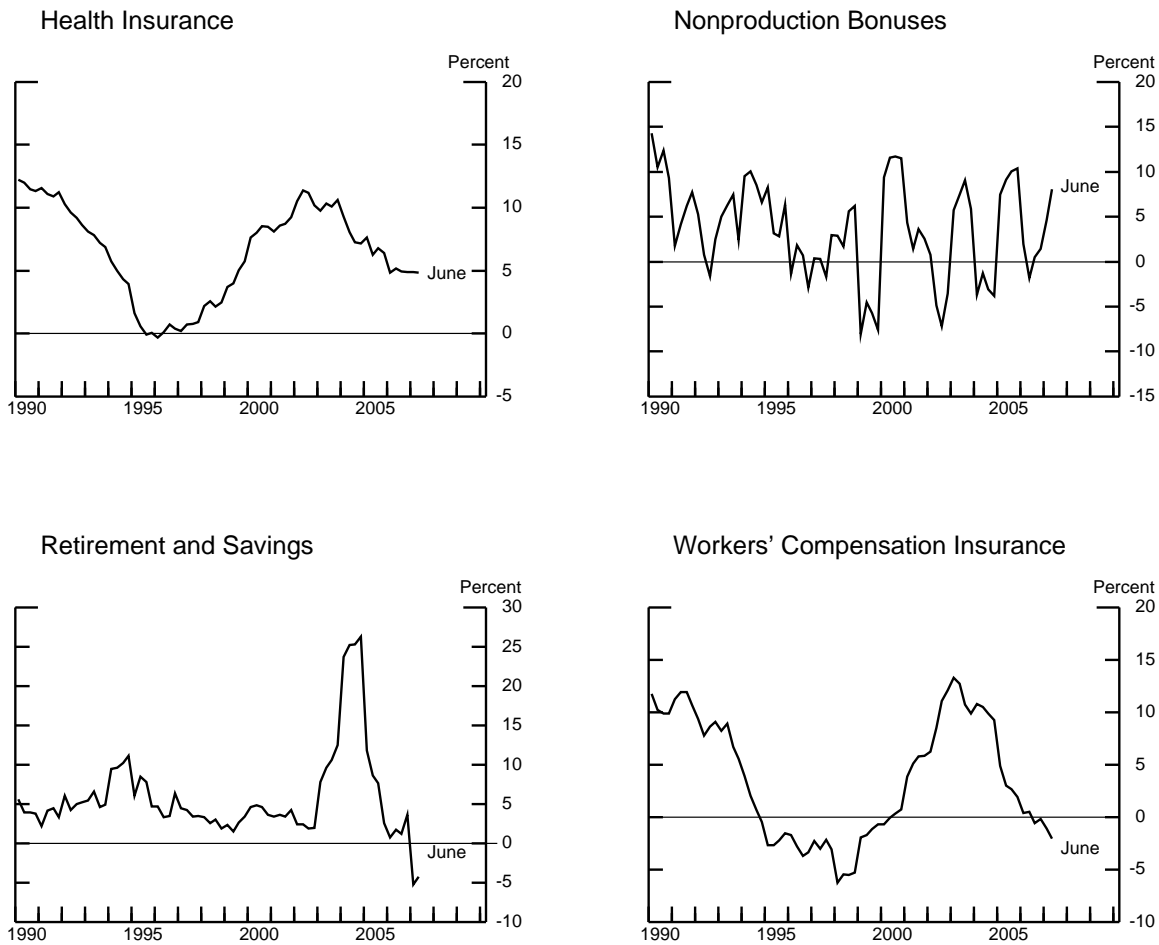
The employment cost index for hourly compensation of private industry workers rose at an annual rate of $3\frac{1}{2}$ percent in the three months ending in June, compared with an annual rate of $2\frac{1}{4}$ percent in the first quarter of this year. This pickup reflected a modest rebound in employer contributions to retirement and savings plans after a very large drop in the preceding three months. The twelve-month change in private-industry hourly compensation was 3.1 percent in June, up about $\frac{1}{4}$ percentage point from the increase

**Change in Employment Cost Index of Hourly Compensation
for Private-Industry Workers**

Measure	2006			2007	
	June	Sept.	Dec.	Mar.	June
	Quarterly change (compound annual rate) ¹				
Total hourly compensation	3.2	3.6	3.2	2.3	3.5
Wages and salaries	3.2	3.2	3.2	4.3	3.1
Benefits	2.8	4.0	3.6	-1.2	4.3
	12-month change				
Total hourly compensation	2.8	3.0	3.2	3.2	3.1
Wages and salaries	2.8	3.0	3.2	3.6	3.3
Benefits	2.7	2.8	3.1	2.2	2.6

1. Seasonally adjusted by the Bureau of Labor Statistics.

Change in ECI Benefits (confidential)
(Private-industry workers; 12-month change)



over the preceding year. The acceleration is the result of a faster increase in wages and salaries— $3\frac{1}{4}$ percent over the twelve months ending in June, compared with $2\frac{3}{4}$ percent over the year-earlier period. ECI benefits increased at about the same rate in both periods; in the most recent twelve-month period, a marked deceleration in retirement and savings contributions was offset by a sizable acceleration in nonproduction bonuses.

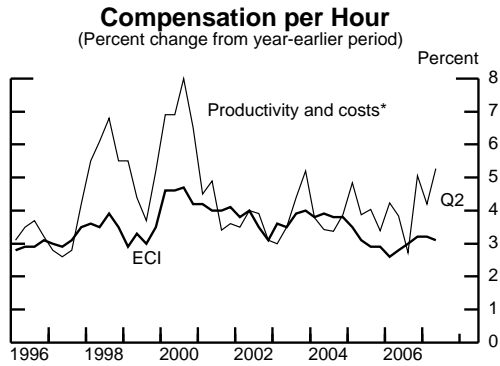
Using the most recent NIPA data, the staff estimates that compensation per hour in the nonfarm business sector rose at an annual rate of 4 percent in the second quarter and was up $5\frac{1}{4}$ percent from four quarters earlier. This four-quarter change is noticeably above the downward-revised gain of $3\frac{3}{4}$ percent posted over the preceding four quarters. Combined with a deceleration in output per hour over the past year, the compensation data imply that unit labor costs have continued to trend up, with the latest four-quarter change at $4\frac{1}{2}$ percent. As a result, the markup of nonfarm business prices over unit labor costs has fallen back somewhat from its peak last year, but it remains well above its long-run average.

Hourly Compensation and Unit Labor Costs

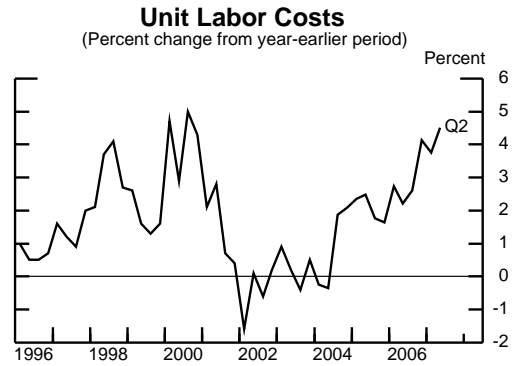
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

Category	2005:Q2 to 2006:Q2	2006:Q2 to 2007:Q2	2006		2007	
			Q3	Q4	Q1	Q2
<i>Compensation per hour</i> Nonfarm business	3.8	5.3	1.4	12.4	3.6	4.0
<i>Unit labor costs</i> Nonfarm business	2.2	4.5	3.0	10.4	2.9	2.0

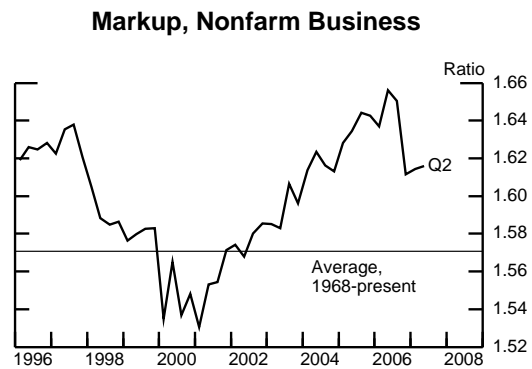
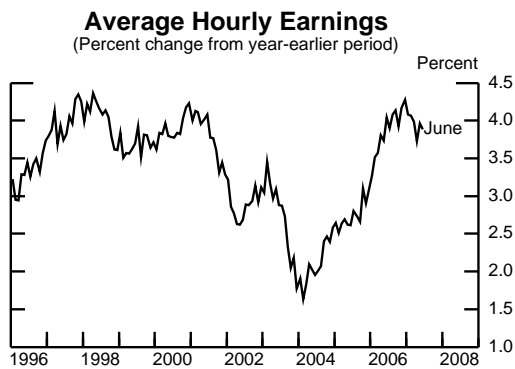
Note. Staff estimates. Output and compensation are derived from the annual revision to the national income and product accounts. However, output and compensation for 2007:Q2 and hours for 2006:Q4, 2007:Q1, and 2007:Q2 are staff estimates. Before 2006:Q4, the level of hours is published data.



* Values after 2003 are staff estimates.



Note. Values after 2003 are staff estimates.



Note. The markup is the ratio of output price to unit labor costs. Values after 2003 are staff estimates.

Appendix

Annual Revision of the National Income and Product Accounts

The annual revision of the national income and product accounts (NIPA), released on July 27, affected data back to the beginning of 2004. This year's revision mainly reflected the incorporation by the Bureau of Economic Analysis (BEA) of more-comprehensive source data. The four-quarter change in real GDP was revised down 0.3 percentage point in 2004, 0.2 percentage point in 2005, and 0.5 percentage point in 2006.

Downward revisions were fairly widespread by expenditure category and did not noticeably alter the contour of real GDP over the revision period. Real personal consumption expenditures (PCE) are now estimated to have risen 0.3 percentage point per year more slowly during the 2004-06 period, and that change made the largest contribution to the overall revision to real GDP. New information from annual Census surveys also showed that outlays by state and local governments increased noticeably more slowly than previously estimated in all three years. Elsewhere, the revisions included lower estimates of spending for residential investment in 2005 and for equipment and software and business inventories in 2006.

The BEA's changes to its price indexes were generally small. Core PCE inflation was revised up 0.1 percentage point in both 2005 and 2006, with market-based core PCE inflation up 0.1 percentage point in 2006 only. However, the increase in overall GDP prices revised up by a larger amount because of a sizable upward revision to residential construction prices in 2005.

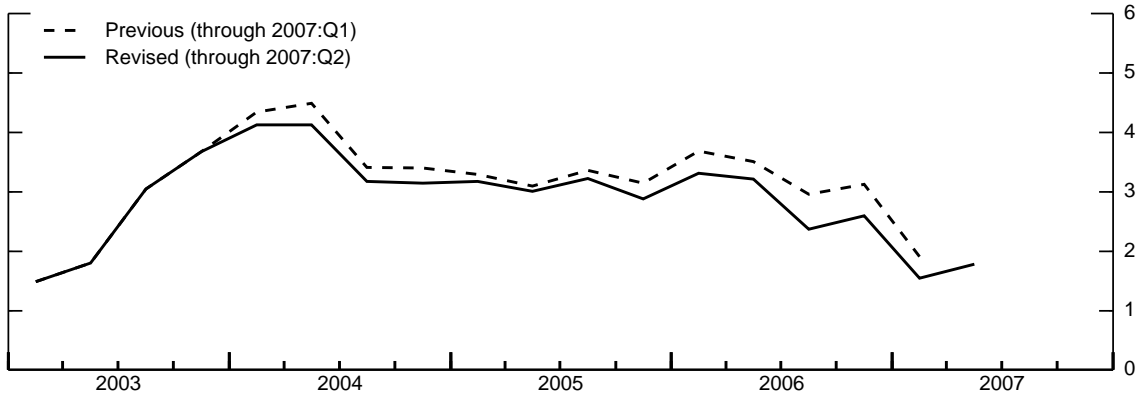
On the income side of the accounts, the average increase in gross domestic income was revised down by about the same amount as GDP; the increase in GDI is still reported to have exceeded the increase in GDP by an average of 0.3 percentage point per year over the 2004-06 period. Real disposable personal income is now estimated to have risen considerably faster because higher estimates of personal interest and dividend income (derived from Internal Revenue Service data) more than offset a downward revision to employee compensation. This higher income, together with the downward revisions to PCE, led the personal saving rate to be revised up 1¾ percentage points, to 1.1 percent by the first quarter of 2007. Corporate profits were revised up in 2004 and 2005 but were revised down considerably in 2006; as a result, corporate profits as a share of GNP are now reported to have increased only modestly last year (and to have declined in the fourth quarter). Much of last year's downward revision to profits stemmed from a revision to the capital consumption adjustment—that is, to new BEA estimates indicating that economic depreciation had revised up relative to companies' reported depreciation. In addition, data from firms' financial reports indicated a much flatter trajectory for book profits over 2006 and into the first quarter of 2007 than previously estimated.

The annual NIPA revision also provided information about the magnitude of upcoming revisions to measures of productivity and compensation per hour in the nonfarm business sector. We now

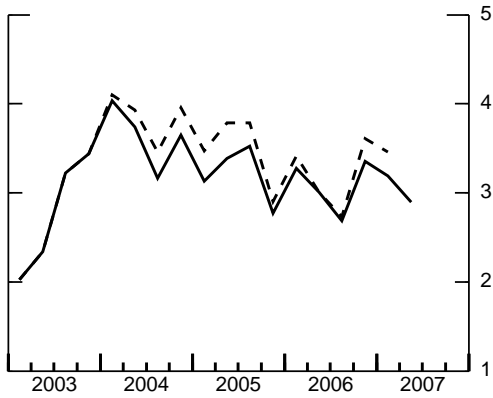
estimate that output per hour in the nonfarm business sector rose at an annual rate of about 1-3/4 percent during 2004 and 2005 and about 1 percent in 2006; these estimates for 2005 and 2006 are 0.4 percentage point and 0.7 percentage point, respectively, lower than reported earlier. In addition, we estimate that increases in compensation per hour in the nonfarm business sector will be revised down through 2006, though by less than productivity. The quarterly pattern of increases in compensation per hour now appears to be somewhat smoother than in the data as currently published, but it remains highly erratic.

Annual Revision to the National Income and Product Accounts
(Four-quarter percent change)

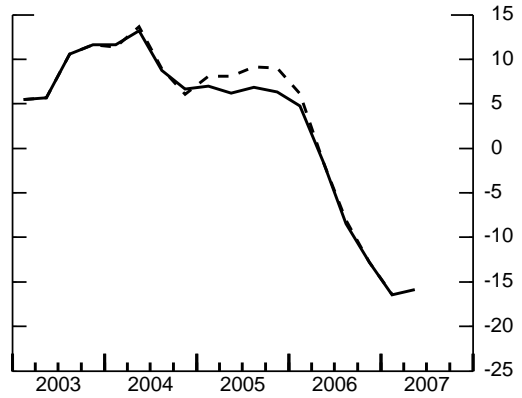
Real GDP



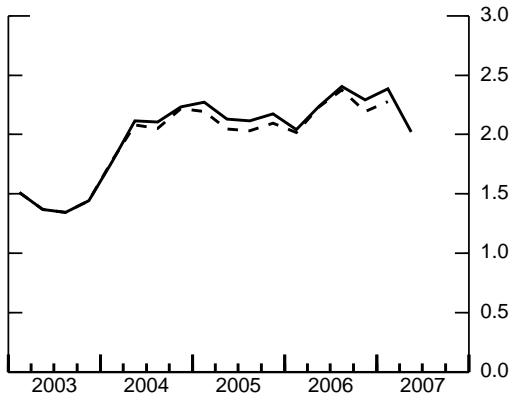
Real Personal Consumption Expenditures



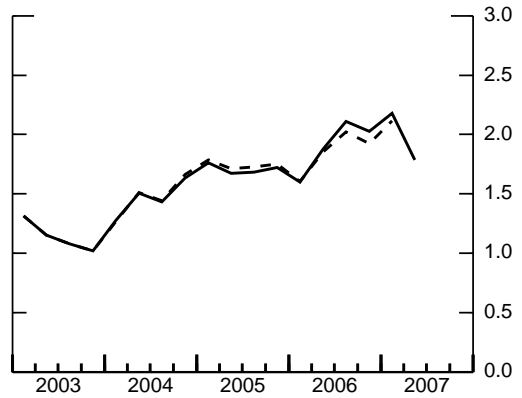
Real Residential Investment



Core PCE Prices

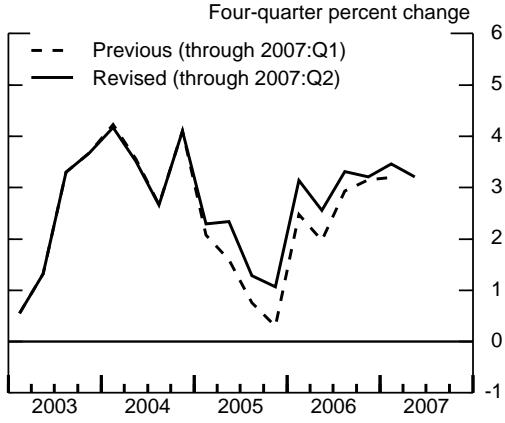


Market-Based Core PCE Prices

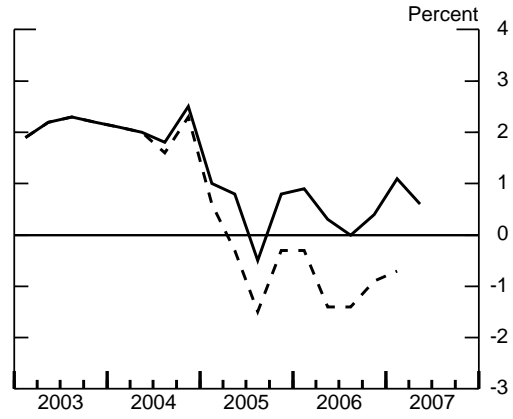


Annual Revision to the National Income and Product Accounts

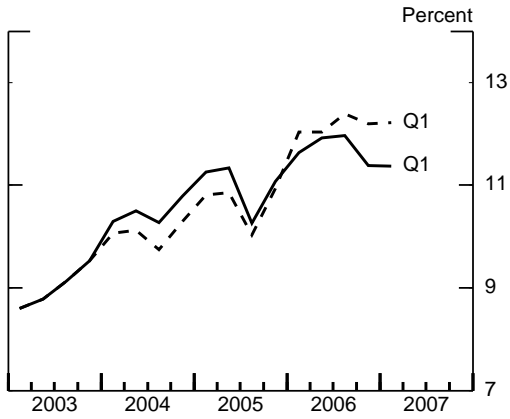
Real DPI



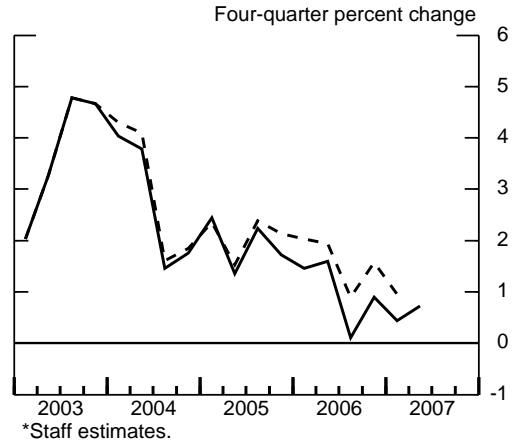
Personal Saving Rate



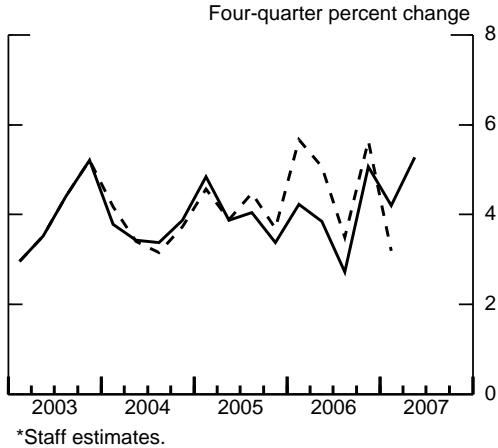
Profits as a Share of GNP



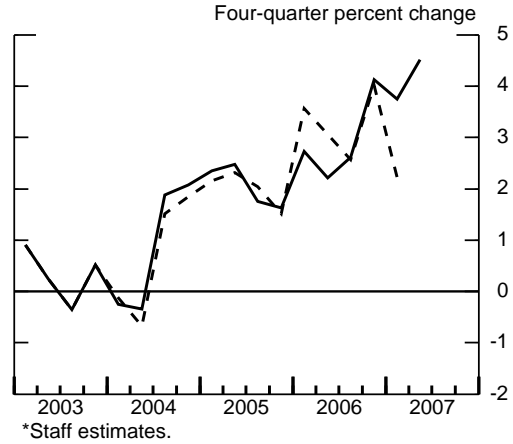
NFB Output per Hour*



Compensation per Hour*



Unit Labor Costs*



Domestic Financial Developments

III-T-1
Selected Financial Market Quotations
(One-day quotes in percent except as noted)

Instrument	2004	2006	2007		Change to Aug. 1 from selected dates (percentage points)		
	June 28	June 29	June 27	Aug. 1	2004 June 28	2006 June 29	2007 June 27
<i>Short-term</i>							
FOMC intended federal funds rate	1.00	5.25	5.25	5.25	4.25	.00	.00
Treasury bills ¹							
3-month	1.36	4.88	4.64	4.75	3.39	-.13	.11
6-month	1.74	5.06	4.75	4.76	3.02	-.30	.01
Commercial paper (A1/P1 rates) ²							
1-month	1.28	5.27	5.25	5.26	3.98	-.01	.01
3-month	1.45	5.37	5.26	5.23	3.78	-.14	-.03
Large negotiable CDs ¹							
3-month	1.53	5.47	5.34	5.33	3.80	-.14	-.01
6-month	1.82	5.59	5.36	5.30	3.48	-.29	-.06
Eurodollar deposits ³							
1-month	1.29	5.33	5.31	5.32	4.03	-.01	.01
3-month	1.51	5.49	5.34	5.35	3.84	-.14	.01
Bank prime rate	4.00	8.25	8.25	8.25	4.25	.00	.00
<i>Intermediate- and long-term</i>							
U.S. Treasury ⁴							
2-year	2.88	5.26	4.94	4.59	1.71	-.67	-.35
5-year	3.97	5.15	4.95	4.59	.62	-.56	-.36
10-year	4.90	5.28	5.16	4.86	-.04	-.42	-.30
U.S. Treasury indexed notes ⁵							
5-year	1.60	2.51	2.67	2.39	.79	-.12	-.28
10-year	2.26	2.61	2.70	2.44	.18	-.17	-.26
Municipal general obligations (Bond Buyer) ⁶	5.01	4.71	4.63	4.47	-.54	-.24	-.16
Private instruments							
10-year swap	5.21	5.81	5.67	5.48	.27	-.33	-.19
10-year FNMA ⁷	5.38	5.59	5.49	5.38	.00	-.21	-.11
10-year AA ⁸	5.60	6.20	6.11	6.13	.53	-.07	.02
10-year BBB ⁸	6.25	6.74	6.56	6.59	.34	-.15	.03
10-year high yield ⁸	8.41	8.74	8.44	9.26	.85	.52	.82
Home mortgages (FHLMC survey rate)							
30-year fixed	6.21	6.78	6.67	6.68	.47	-.10	.01
1-year adjustable	4.19	5.82	5.65	5.59	1.40	-.23	-.06

Stock exchange index	Record high		2006	2007		Change to Aug. 1 from selected dates (percent)		
	Level	Date	June 29	June 27	Aug. 1	Record high	2006 June 29	2007 June 27
Dow Jones Industrial	14,000	7-19-07	11,191	13,428	13,362	-4.56	19.40	-.49
S&P 500 Composite	1,553	7-19-07	1,273	1,506	1,466	-5.62	15.16	-2.69
Nasdaq	5,049	3-10-00	2,174	2,605	2,554	-49.41	17.45	-1.98
Russell 2000	856	7-13-07	714	838	778	-9.10	8.90	-7.22
Wilshire 5000	15,701	7-13-07	12,846	15,233	14,755	-6.02	14.87	-3.13

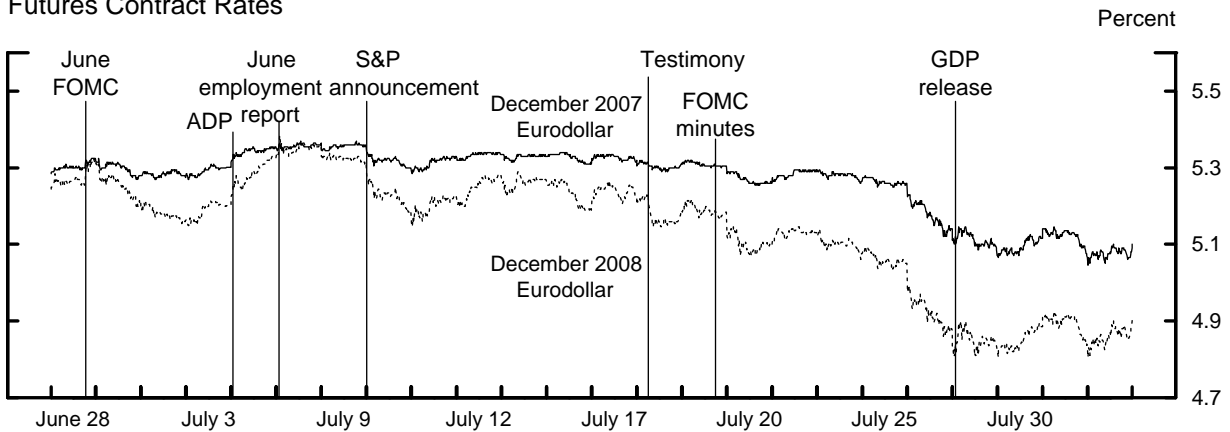
1. Secondary market.
2. Financial commercial paper.
3. Bid rates for Eurodollar deposits collected around 9:30 a.m. eastern time.
4. Derived from a smoothed Treasury yield curve estimated using off-the-run securities.
5. Derived from a smoothed Treasury yield curve estimated using all outstanding securities and adjusted for the carry effect.
6. Most recent Thursday quote.
7. Constant-maturity yields estimated from Fannie Mae domestic noncallable coupon securities.
8. Derived from smoothed corporate yield curves estimated using Merrill Lynch bond data.

NOTES:

June 28, 2004, is the day before the most recent policy tightening began.
June 29, 2006, is the day the most recent policy tightening ended.
June 27, 2007, is the day before the most recent FOMC announcement.

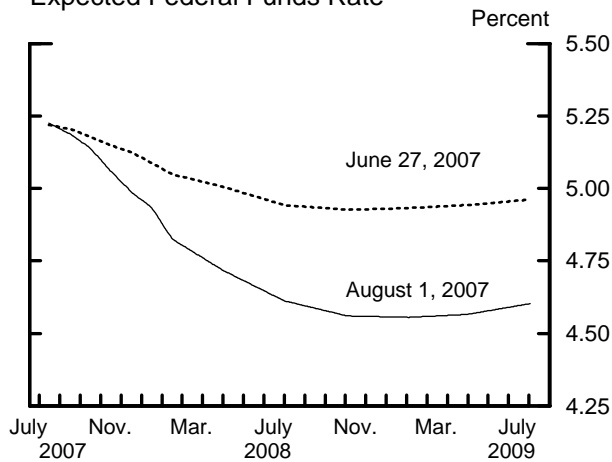
Policy Expectations and Treasury Yields

Futures Contract Rates



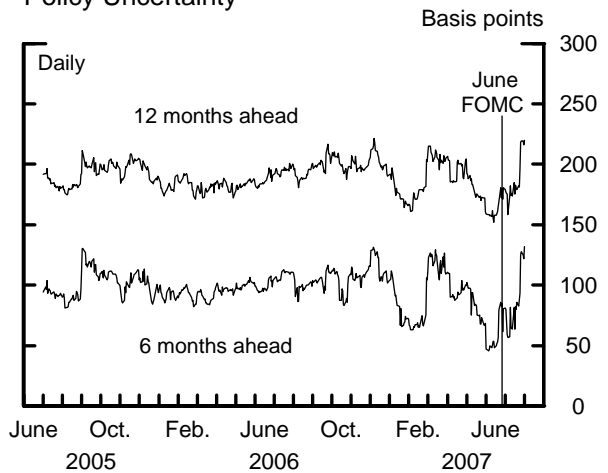
Note. 5-minute intervals.

Expected Federal Funds Rate



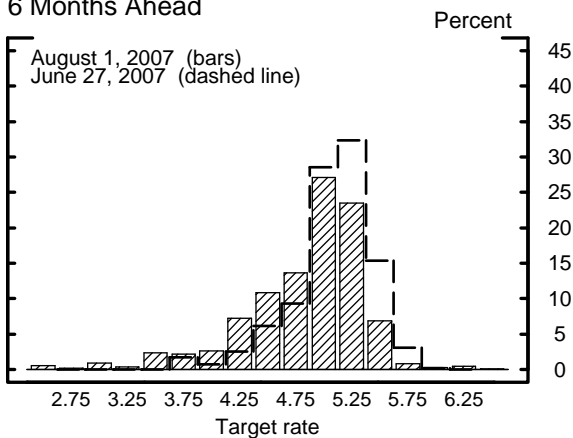
Note. Estimates from federal funds and Eurodollar futures, with an allowance for term premia and other adjustments.

Policy Uncertainty



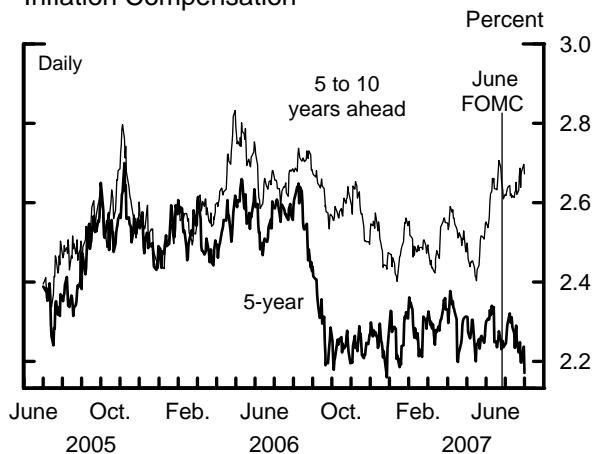
Note. Width of a 90 percent confidence interval for the federal funds rate computed from the term structures for both the expected federal funds rate and implied volatility.

Implied Distribution of Federal Funds Rate 6 Months Ahead



Note. Based on the distribution of the 3-month Eurodollar rate 6 months ahead (adjusted for a term premium) as implied by options on Eurodollar futures contracts.

Inflation Compensation



Note. Estimates based on smoothed nominal and inflation-indexed Treasury yield curves and adjusted for the indexation-lag effect.

Domestic Financial Developments

Overview

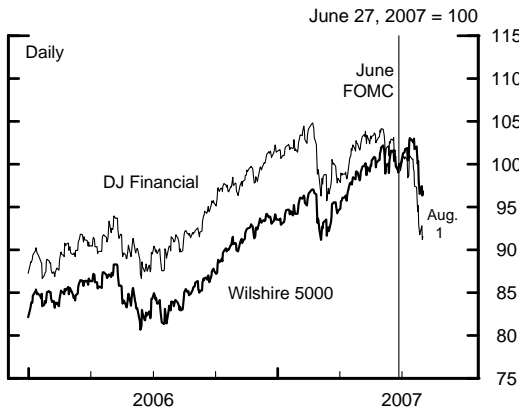
Mounting concerns about subprime mortgage performance and credit risk more broadly reverberated in financial markets during the intermeeting period. The value of securities tied to subprime mortgages plunged, and issuance of such securities slowed sharply. Risk spreads on corporate bonds widened notably, although business credit quality has yet to show any deterioration. A number of planned issues of speculative-grade bonds and leveraged loans, intended predominantly to finance leveraged buyouts (LBOs), were postponed or restructured, but issuance of investment-grade corporate bonds appeared little affected. Broad equity-price indexes fell, on net, over the period despite solid second-quarter earnings reports. Expectations for the federal funds rate and yields on Treasury securities declined considerably even though incoming economic data were generally seen as mixed.

Policy Expectations and Interest Rates

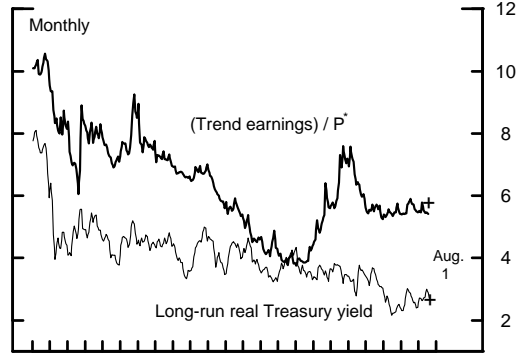
Market participants largely anticipated the FOMC's decision at its June meeting to leave the target federal funds rate unchanged. However, the accompanying statement expressed greater concern about inflation than investors reportedly had foreseen and caused the expected path for policy to edge higher. In addition, policy expectations were boosted a bit by some favorable economic news early in the intermeeting period. However, money market futures rates declined a little in the wake of the Chairman's semiannual testimony to Congress, as investors reportedly focused on the downward revision to the Committee's central tendency forecast for real GDP growth. Rates fell further amid growing apprehension about the risk to economic growth associated with the difficulties in the subprime mortgage market and the market for low-rated corporate credits. Federal funds futures currently imply a small probability of a rate cut at the August FOMC meeting and roughly a 40 percent chance of an easing by the September meeting. Further out, investors have marked down their policy expectations even more and now appear to expect about 70 basis points of easing by the end of 2008, up from about 30 basis points at the time of the last FOMC meeting. By contrast, primary dealers in the Desk's survey put lower odds on the prospects for near-term policy easing than do futures market participants: Dealers reported that they placed virtually no odds on a rate cut at the August meeting and expect only about 15 basis points of easing between now and the end of next year. Measures of policy uncertainty derived from options on Eurodollar futures climbed notably over the intermeeting period, and the implied distribution of the federal funds rate became more skewed toward lower rates.

Corporate Yields, Risk Spreads, and Stock Prices

Wilshire 5000 and Dow Jones Financial Index



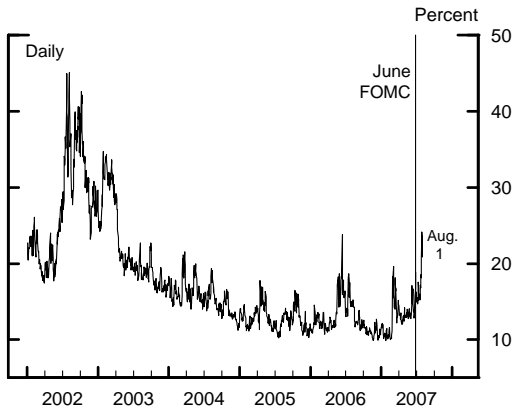
Ratio of Trend Earnings to Price for S&P 500 and Long-Run Treasury Yield



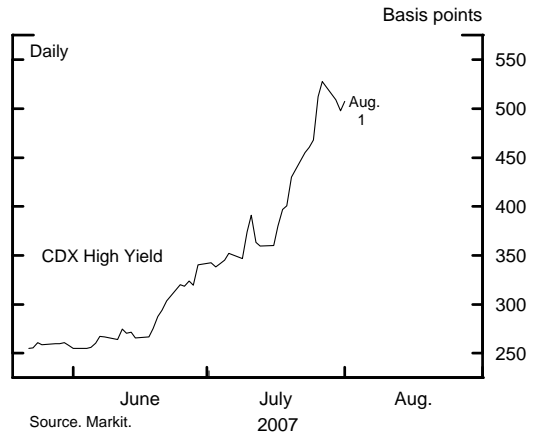
+ Denotes the latest observation using daily interest rates and stock prices and latest earnings data from I/B/E/S.

* Trend earnings are estimated using analysts' forecasts of year-ahead earnings from I/B/E/S.

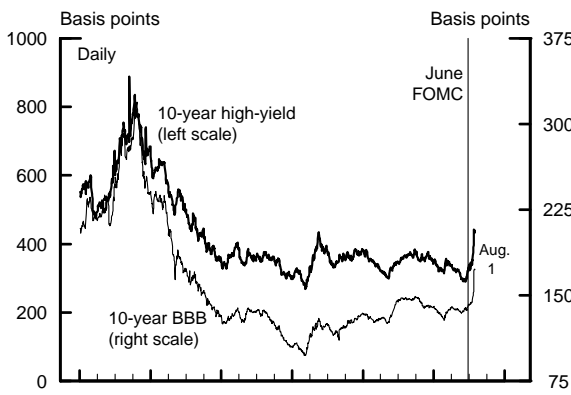
Implied Volatility on S&P 500 (VIX)



Credit Default Swap Spread

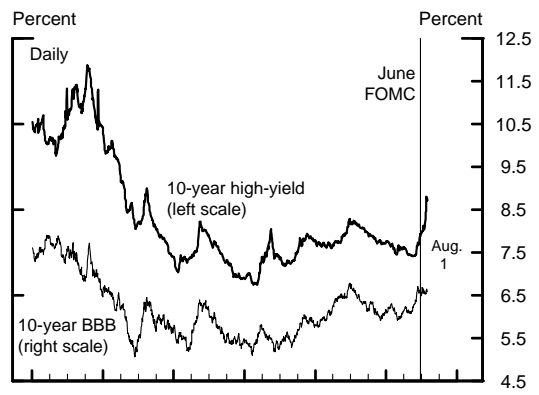


Corporate Bond Spreads



Note. Measured relative to comparable-maturity Treasuries.

Corporate Bond Yields



Note. Yields from smoothed yield curves based on Merrill Lynch bond data.

On balance, two- and ten-year nominal Treasury yields fell 35 and 30 basis points, respectively, over the intermeeting period, in part because of the decline in the expected path of the funds rate. A decline in estimated term premiums and a notable increase in swap spreads since the June meeting are consistent with reports that safe-haven demands also contributed to the decline in Treasury yields. Yields on Treasury inflation-protected securities declined somewhat less than their nominal counterparts, thereby leaving inflation compensation a bit lower on net.

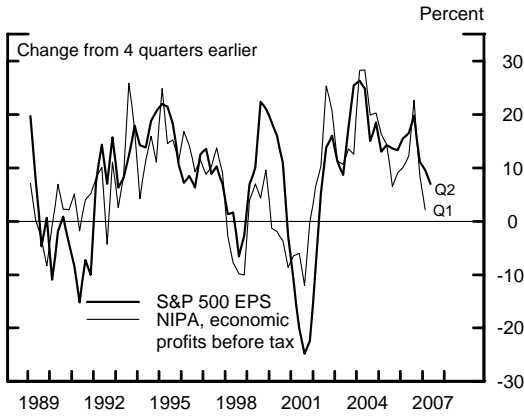
Stock Prices and Corporate Interest Rates

Broad stock price indexes declined about 3 percent, on net, since the June meeting despite generally solid second-quarter earnings reports. Share prices of financial firms fell 9 percent, partly reflecting concerns about exposures to subprime mortgages and about the effect of a potential slowdown in merger activity on operating profitability. Share prices for retailers dropped 5 percent on a number of warnings that sales in the second quarter were lower than expected. Amid declining share prices and Treasury yields, the spread between the twelve-month forward trend earnings-price ratio for S&P 500 firms and a real long-run Treasury yield—a rough gauge of the equity risk premium—widened somewhat. Implied volatility on the S&P 500 index jumped to the top of its range over the past few years.

Conditions in corporate credit markets tightened substantially over the intermeeting period. Spreads on a traded index comprising 100 of the most liquid speculative-grade credit default swaps (CDS) rose about 185 basis points, as investors pulled back from riskier assets. Spreads on CDS were also reportedly boosted by a flood of hedging demands from institutions that had committed to underwriting LBOs. Spreads on speculative-grade bonds increased about 110 basis points since the June meeting and now stand about 150 basis points above their lows in mid-June. Investment-grade bond spreads rose about 30 basis points. Speculative-grade and investment-grade bond spreads are now at the top of their ranges over the past four years but are still below their peaks in 2002. Because Treasury yields declined notably since the June meeting, investment-grade yields are about unchanged despite the rise in spreads. Liquidity in the CDS and corporate bond markets appeared to remain adequate.

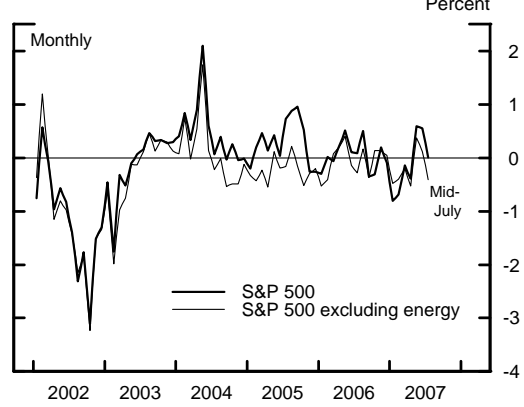
Corporate Earnings and Credit Quality

Corporate Earnings Growth



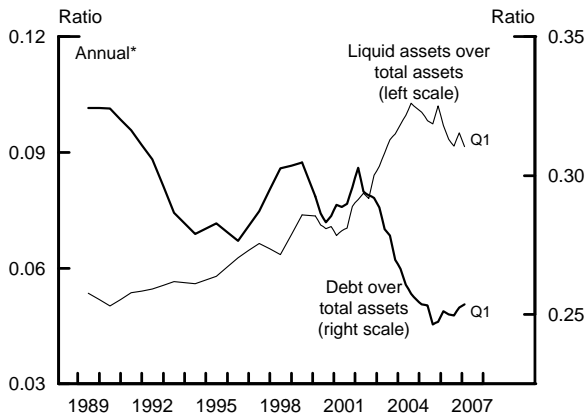
Source: I/B/E/S for S&P 500 earnings per share.

Revisions to Expected S&P 500 Earnings



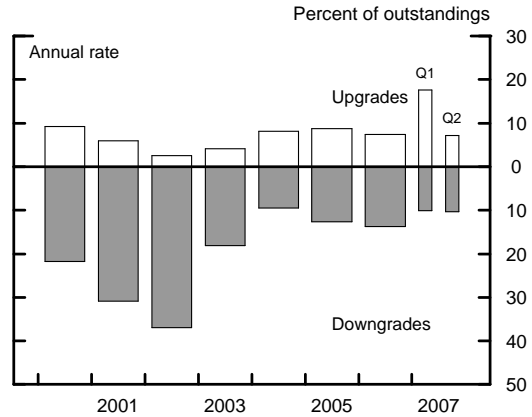
Note. Index is a weighted average of the percent change in the consensus forecasts of current-year and following-year EPS for a fixed sample.

Financial Ratios for Nonfinancial Corporations



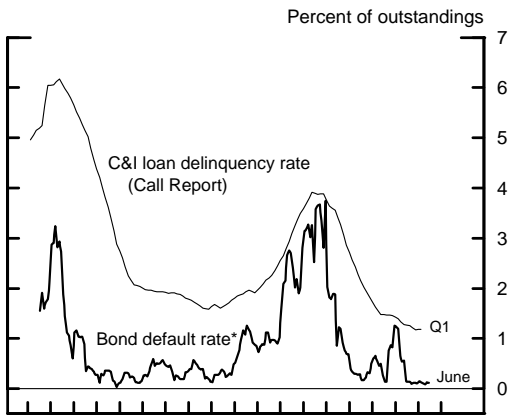
* Data are quarterly starting in 2000:Q1. Source. Calculated with Compustat data.

Bond Ratings Changes of Nonfinancial Companies



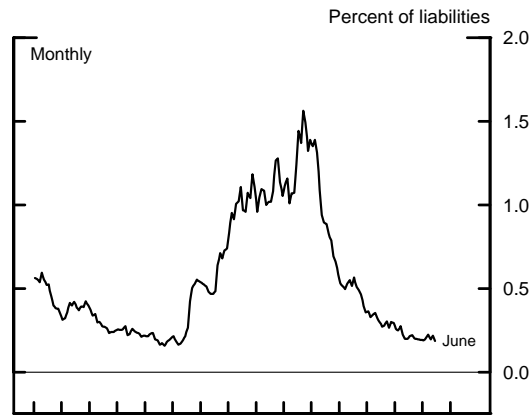
Source. Calculated with data from Moody's Investors Service.

Selected Default and Delinquency Rates



* 6-month moving average, from Moody's Investors Service.

Expected Year-Ahead Defaults



Note. Firm-level estimates of default weighted by firm liabilities as a percent of total liabilities, excluding defaulted firms. Source. Moody's KMV.

Business Finance

Gross Issuance of Securities by U.S. Corporations

(Billions of dollars; monthly rates, not seasonally adjusted)

Type of security	2003	2004	2005	2006		2007		
				H1	H2	Q1	Q2	July ^p
<i>Nonfinancial corporations</i>								
Stocks ¹	3.7	5.4	4.6	5.2	4.1	5.9	5.1	1.5
Initial public offerings	.4	1.6	1.7	1.9	1.7	1.3	2.1	.6
Seasoned offerings	3.3	3.8	2.8	3.3	2.4	4.6	3.1	.9
Bonds ²	31.6	22.7	19.1	30.3	29.5	31.9	41.6	13.0
Investment grade	15.9	8.2	8.4	14.4	11.6	13.0	15.0	9.0
Speculative grade	11.3	9.7	6.4	8.4	7.6	13.0	17.8	2.2
Other (sold abroad/unrated)	4.3	4.9	4.3	7.6	10.4	5.9	8.8	1.8
<i>Memo</i>								
Net issuance of commercial paper ³	-3.4	1.5	-4	3.4	4.4	-.1	2.6	1.4
Change in C&I loans at commercial banks ^{3,4}	-7.7	3.2	10.0	14.5	11.2	8.6	14.4	16.4
<i>Financial corporations</i>								
Stocks ¹	6.6	6.9	5.0	4.4	6.2	8.7	9.4	1.0
Bonds ²	111.1	139.3	176.3	190.2	185.3	208.6	197.7	120.0

Note. Components may not sum to totals because of rounding.

1. Excludes private placements and equity-for-equity swaps that occur in restructurings.

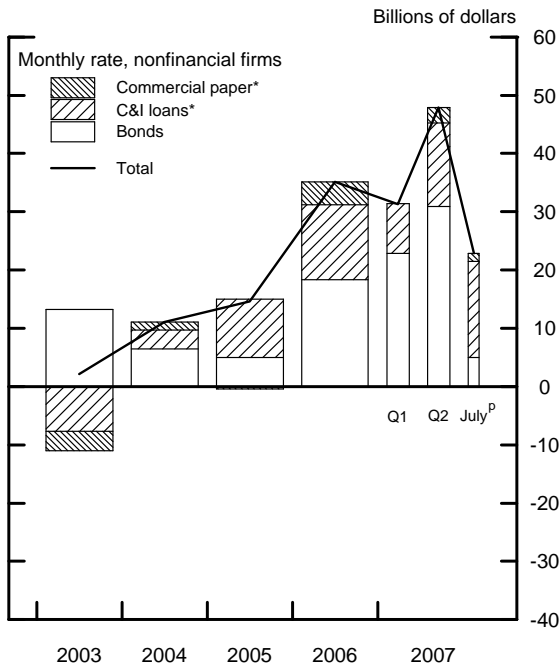
2. Data include regular and 144a private placements. Bond totals reflect gross proceeds rather than par value of original discount bonds. Bonds are categorized according to Moody's bond ratings or to Standard & Poor's if unrated by Moody's.

3. End-of-period basis, seasonally adjusted.

4. Adjusted commercial bank credit data.

p Preliminary.

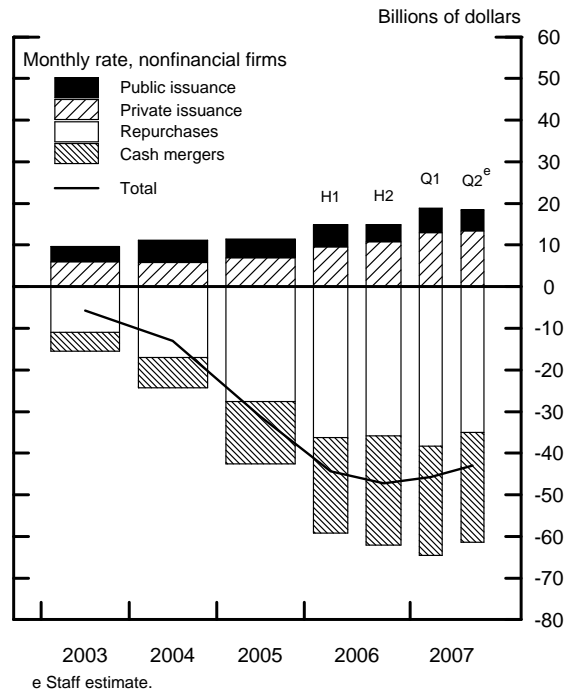
Selected Components of Net Debt Financing



* Seasonally adjusted, period-end basis.

p Preliminary.

Components of Net Equity Issuance



e Staff estimate.

Corporate Earnings and Credit Quality

Second-quarter earnings reports have generally been solid. However, most homebuilders disclosed substantial second-quarter losses, which stemmed in part from falling land prices, and several financial firms reported losses on assets related to subprime mortgages. With about three-quarters of reports in hand and analysts' estimates for the rest, the staff projects that earnings per share for S&P 500 firms will come in about 7 percent above year-earlier levels. As usual, most announcements exceeded analysts' forecasts. Regarding the near-term outlook, the revision index of analysts' forecasts of year-ahead earnings for S&P 500 firms was near zero in July.

Although some of our indicators are a bit stale, corporate credit quality appears to have remained strong overall. Liquidity of nonfinancial corporate balance sheets stayed high by historical standards in the first quarter, and leverage for that sector remained low. Rating downgrades on corporate bonds continued to be modest in the second quarter, and the realized six-month trailing bond default rate hovered near zero in June. KMV's aggregate year-ahead expected bond default rate stayed near record lows in June; although we anticipate some increase in July because of the decline in stock prices and the rise in volatility, the near-term outlook for corporate credit quality implied by the KMV measure almost surely remains favorable.

Business Finance

The influence of tighter financial conditions in corporate credit markets has been concentrated in financings slated for LBOs. Continuing the trend that began in late June, a number of high-yield bond and leveraged loan issues intended to finance LBOs were delayed or restructured over the intermeeting period. Issuance of high-yield bonds slowed but did not stop in July. Leveraged loan issuance also fell considerably, as investors have become uncertain about the valuation of securities issued by structured entities (such as collateralized loan obligations and collateralized debt obligations), the primary buyers of leveraged loans in recent years. Investment-grade bond issuance appeared little affected, although one investment-grade firm postponed a deal scheduled to come to market on July 26, a day of particularly high volatility in financial markets. Commercial paper outstanding posted a modest gain in July. C&I loan growth through mid-July picked up from an already solid clip. According to industry reports, underwriting banks have been forced to keep on their balance sheets loans that they were

unable to place with investors. Overall, net debt financing stepped down in July from its torrid second-quarter pace but remained moderate.¹

Gross public equity issuance by nonfinancial corporations also fell off in July, in line with typical seasonal patterns. Private equity issuance is estimated to have picked up in the second quarter on the strength of LBOs. Even so, net equity issuance continued to be deeply negative, as share repurchases and retirements from cash-financed mergers and acquisitions both held at near-record paces. In July, tighter financial conditions for speculative-grade firms weighed on merger and acquisition activity, particularly LBOs, portending a slowdown in retirements, and to a lesser extent, private issuance.

Commercial Real Estate

Commercial mortgage debt is estimated to have expanded briskly again in the second quarter, and the issuance calendar for commercial-mortgage-backed securities (CMBS) suggests solid growth early in the third quarter.

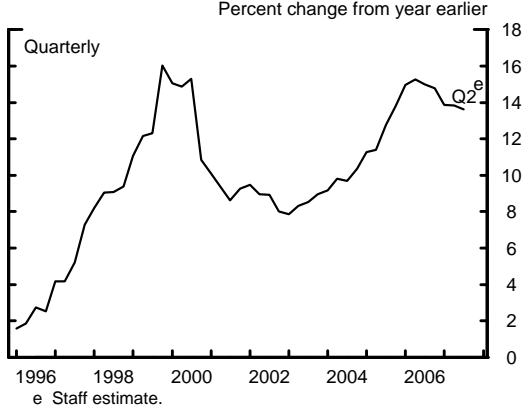
Spreads of rates on investment-grade CMBS over those on comparable-maturity Treasury securities have risen sharply over the intermeeting period, and the spread on the BBB-rated tranche now stands at its highest level since the fall of 1998. CMBS spreads rose earlier this year as demand fell from the sponsors of collateralized debt obligations (CDOs). Over the past couple of months, spreads have been volatile but trended up sharply as investors and rating agencies became increasingly concerned about the higher leverage on recently securitized mortgages. The most recent spike in late July may reflect increased anxiety about structured products in general.

The delinquency rate on CMBS ticked down in June to the lowest level recorded for this series. Delinquency rates on commercial mortgages held at life insurance companies remained negligible in the first quarter, whereas the delinquency rate on commercial mortgages held at commercial banks rose a bit because of deterioration in the performance of loans for multifamily properties and for construction and land development. Although the vacancy rate on commercial properties edged up in the second quarter, it remained at a relatively low level, consistent with the moderate gains in rents. Increases in commercial property prices relative to operating income in the second quarter led to another decline in the ratio of net operating income to property prices, an indicator of the rate of return on commercial real estate. As a result, the spread of this

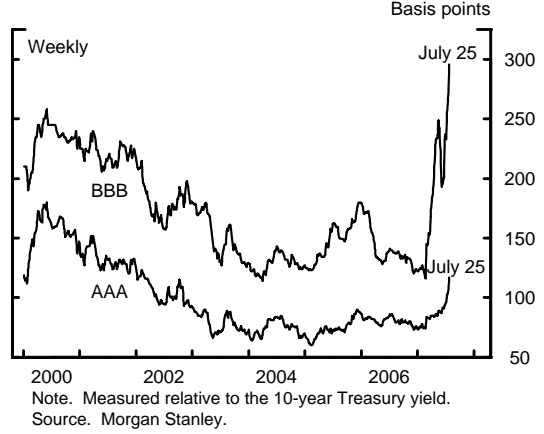
¹ Because of data limitations, the net debt financing measure used here excludes leveraged loan issuance held by institutional investors.

Commercial Real Estate

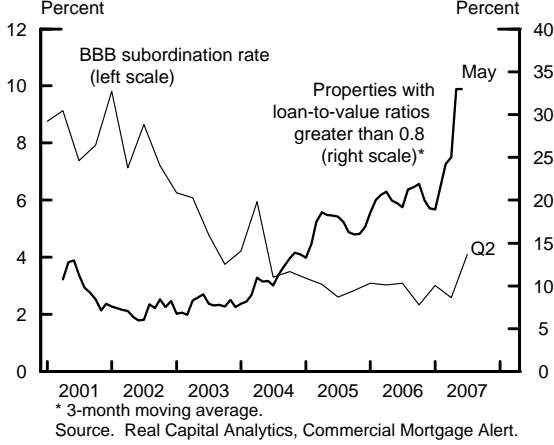
Commercial Mortgage Debt



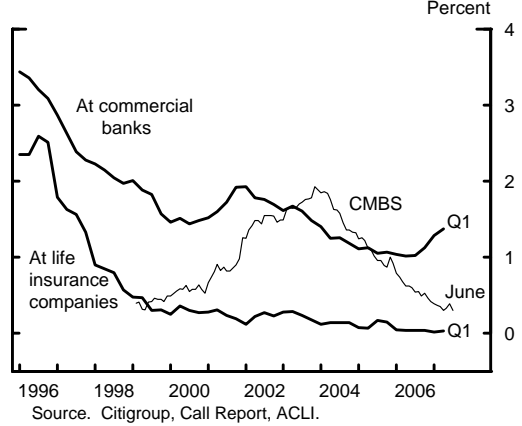
Investment-Grade CMBS Spreads



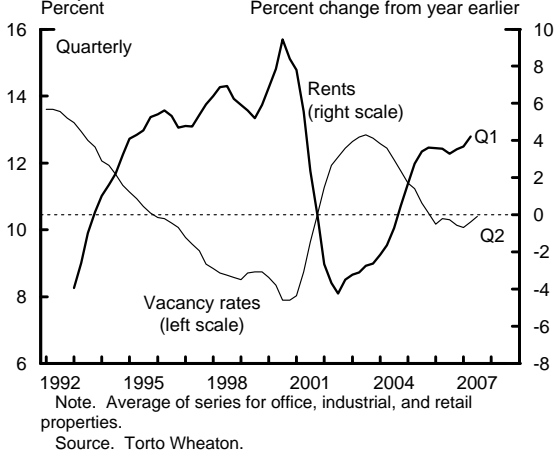
Leverage on Newly Securitized Mortgages



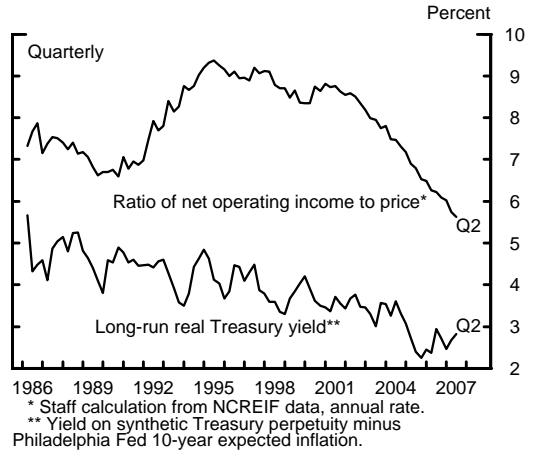
Delinquency Rates on Commercial Mortgages



Rents and Vacancy Rates on Commercial Properties



Commercial Real Estate Valuation



ratio over the real perpetuity Treasury yield, a rough measure of the risk premium on commercial real estate assets, narrowed somewhat in the second quarter to its lowest level since 1991, reflecting continued strong demand for commercial real estate properties.

Household Finance

Over the intermeeting period, interest rates on both fixed-rate and adjustable-rate mortgages for prime borrowers ticked down. Mortgage debt growth is likely to have slowed further in the second quarter because of the decline in home-price growth over the past year. Consumer credit expanded moderately through the year ending in May.

Delinquency rates on consumer loans and prime mortgages—which account for the vast majority of total household debt—remained low through May. Nevertheless, according to the Senior Loan Officer Opinion Survey, a number of banks tightened standards for prime mortgages over the past three months. The delinquency rate on subprime variable-rate mortgages topped 13 percent in June, more than double the low in mid-2005.²

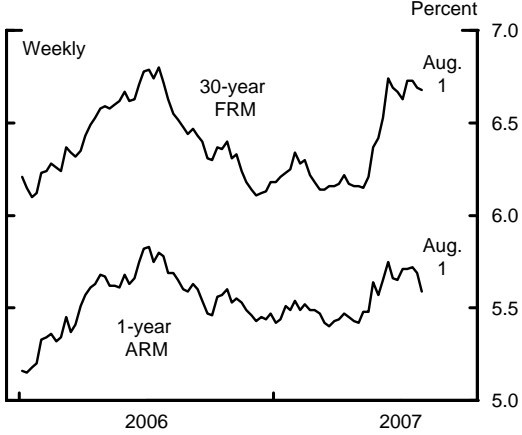
Issuance of subprime-mortgage-backed securities (subprime MBS) has been negligible in July, as underwriters had difficulties placing these securities with investors. Demand from CDOs was reported to be particularly weak, possibly reflecting investor uncertainty about the ratings that MBS-backed tranches of CDOs would receive. Originations of subprime mortgages may have been held down by a further tightening of credit standards on nontraditional and subprime mortgage products, consistent with responses to the July Senior Loan Officer Opinion Survey. Spreads on new issues of subprime MBS over libor climbed further over the intermeeting period after downgrades by Standard & Poor's and Moody's of MBS backed by subprime mortgages originated in the first half of 2006. Standard & Poor's also downgraded some CDOs backed by subprime MBS, including some AAA-rated tranches. Severe liquidity problems at a few large nonprime mortgage lenders contributed to the general sense of investor angst about the mortgage market.

The OFHEO purchase-only index of home prices rose at an annual rate of 2.2 percent in the first quarter, and the available monthly indicators point to little change in that index in

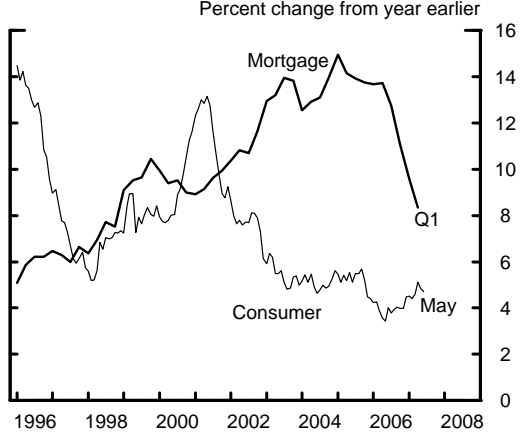
² There was reportedly considerable attention paid to the announcement by a major mortgage lender that it had experienced a rise in delinquencies in the second quarter across all mortgage products, not just subprime loans, and that the housing market may not recover until 2009. However, this report may not be indicative of broad housing market trends but instead may reflect the relatively severe deterioration in the housing market in California, where that lender's business is concentrated.

Household Liabilities

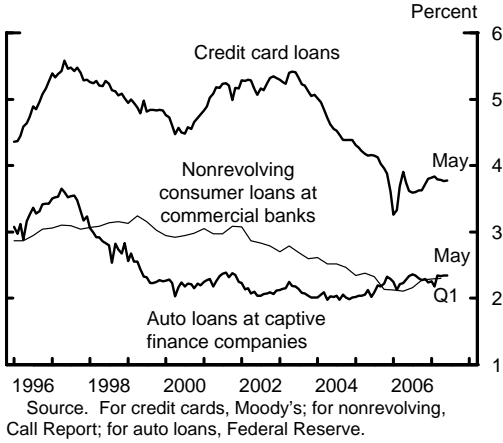
Mortgage Rates



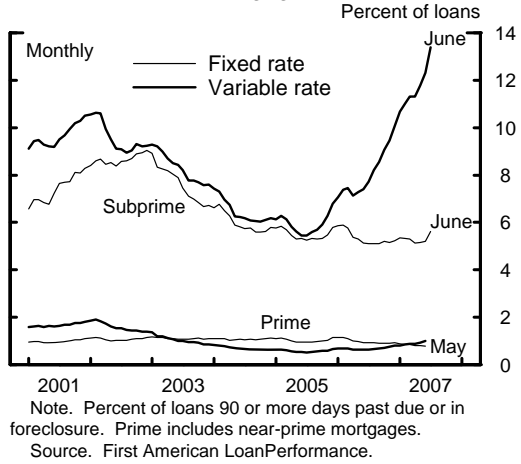
Mortgage Debt and Consumer Credit



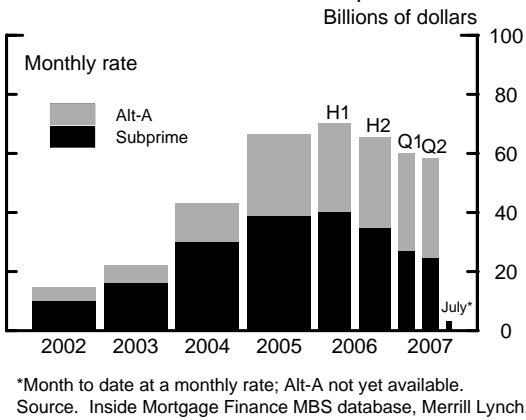
Delinquencies on Consumer Loans



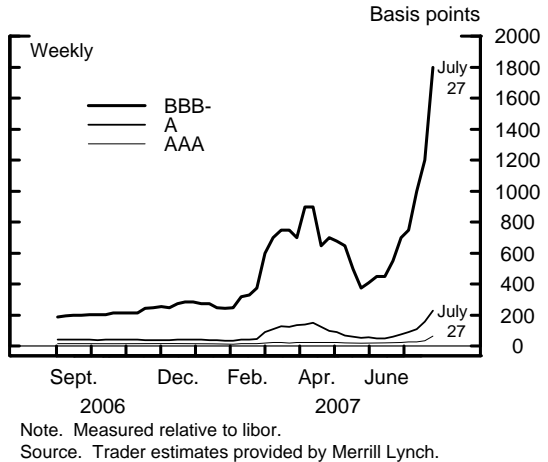
Delinquencies on Mortgages



Gross Issuance of Alt-A and Subprime MBS

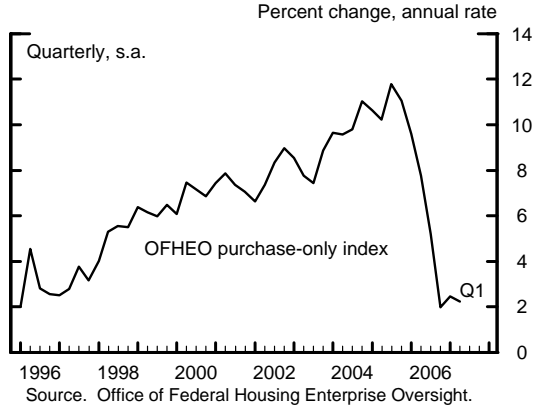


Spreads on New Subprime RMBS Issues

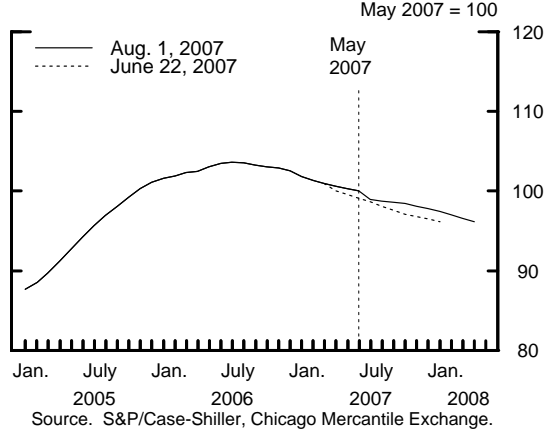


Household Assets

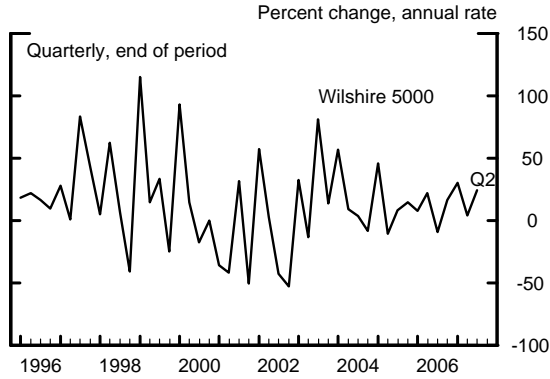
House Prices



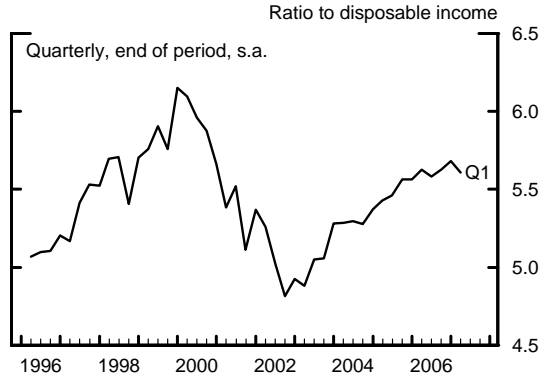
S&P/Case-Shiller House Price Futures



Stock Prices



Net Worth



Net Flows into Long-Term Mutual Funds

(Billions of dollars, monthly rate)

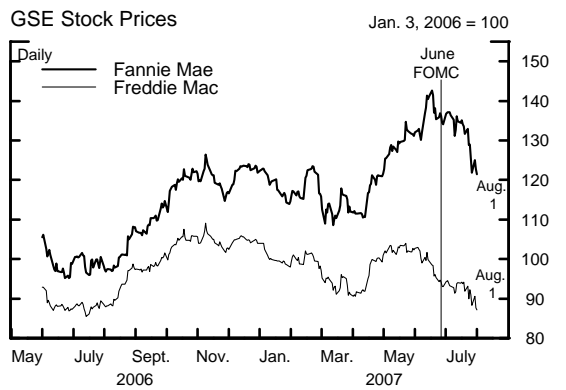
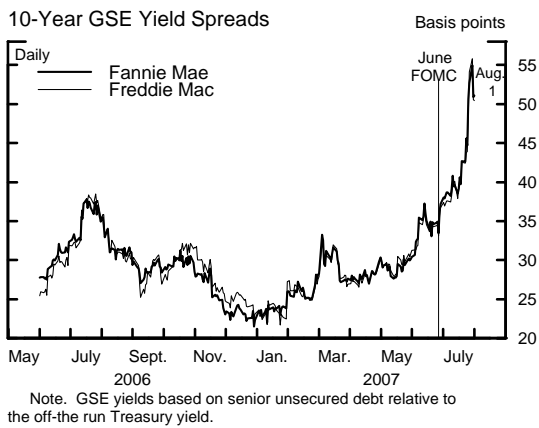
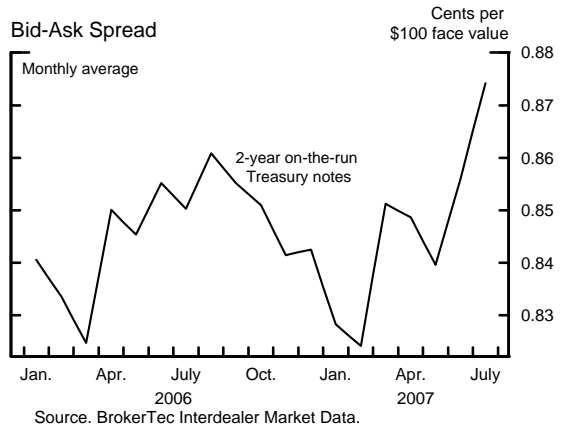
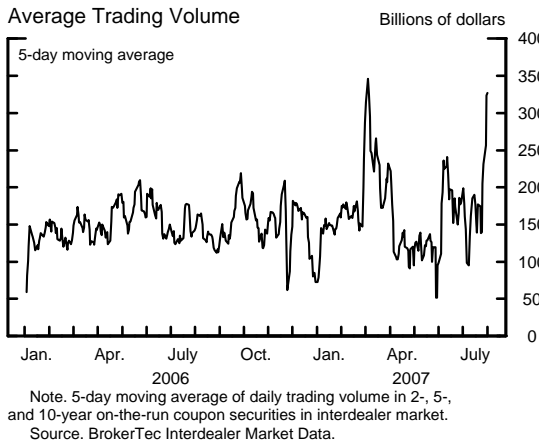
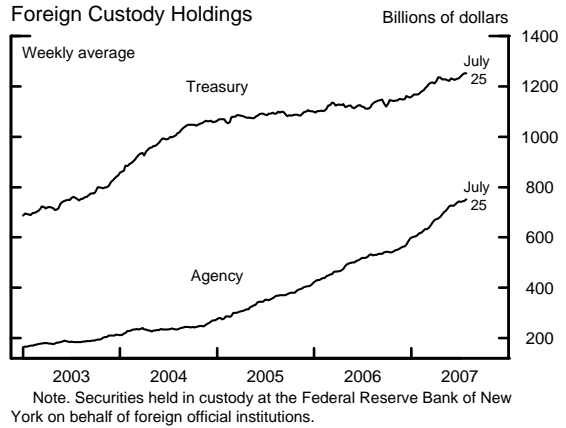
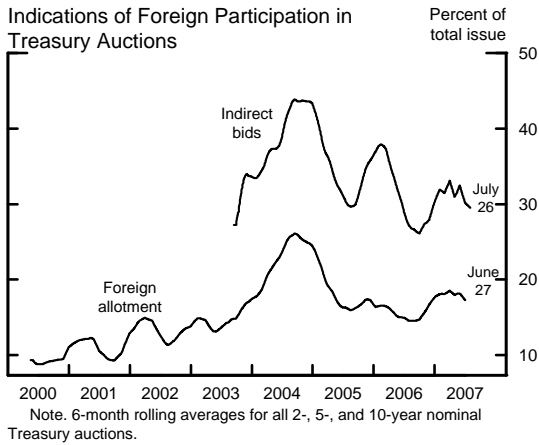
Fund type	2006	2006	2007		2007			Assets June
		Q4	Q1	Q2	May	June	July ^e	
Total long-term funds	18.9	21.6	39.5	24.4	24.6	14.2	24.4	8,852
Equity funds	13.2	11.2	21.2	8.3	1.3	5.5	12.2	6,553
Domestic	0.8	-0.9	6.5	-3.8	-10.1	-3.0	-1.0	4,993
International	12.4	12.1	14.7	12.1	11.4	8.5	13.3	1,560
Hybrid funds	0.6	1.8	3.3	1.9	2.0	1.2	1.9	699
Bond funds	5.1	8.6	15.0	14.1	21.3	7.5	10.3	1,600
High-yield	-0.2	0.5	0.7	-0.2	1.3	-2.4	0.2	163
Other taxable	4.1	6.3	11.4	12.5	16.5	9.4	9.2	1,059
Municipals	1.3	1.8	2.9	1.8	3.6	0.5	0.9	378

Note. Excludes reinvested dividends.

e Staff estimate based on confidential weekly data.

Source. Investment Company Institute.

Treasury and Agency Finance



the second quarter. Futures quotes on the S&P/Case-Shiller home-price index continue to indicate that home prices in ten of the largest metropolitan markets are expected to decline modestly over the next few quarters.

Given the rise in stock prices in the second quarter and our expectation of essentially flat house prices, we estimate that household net worth relative to disposable income increased last quarter, reversing the decline posted in the first quarter. Net flows to long-term mutual funds were robust in June and July, propelled by strong inflows to both international equity and bond funds, while domestic equity funds continued to have net outflows.

Treasury and Agency Finance

Treasury security auctions during the intermeeting period were well received, according to bid-to-cover ratios. Demand from foreign investors appeared to stay strong: The six-month trailing averages of indirect bidding ratios remained robust, and foreign custody holdings at the Federal Reserve Bank of New York edged a bit higher.

Despite the strains in credit markets, Treasury market liquidity remained ample. Trading volume for on-the-run issues was near record highs. Bid-ask spreads widened slightly, on balance, but were within historical norms.

Yield spreads on debt issued by Fannie Mae and Freddie Mac over comparable Treasury securities moved to their widest levels in a few years, reflecting investor concerns regarding their exposure to mortgage products. These concerns also weighed on share prices of these government-sponsored enterprises, which fell roughly 10 percent on net.

In its quarterly refunding statement, the Treasury Department announced that it will offer \$22 billion in new securities at the August refunding, including \$13 billion in ten-year notes and \$9 billion in thirty-year bonds. The Treasury also reported that it expects the current debt ceiling to be reached in early October.

State and Local Government Finance

Gross issuance of long-term municipal bonds fell sharply in July. Short-term issuance is on track to match its average pace over the first half of the year. Rating changes were minimal in July, and the ratio of a representative municipal bond yield to a comparable-maturity Treasury yield stayed near the low end of its range of the past decade, suggesting that the credit quality of municipal bonds remains solid.

State and Local Government Finance

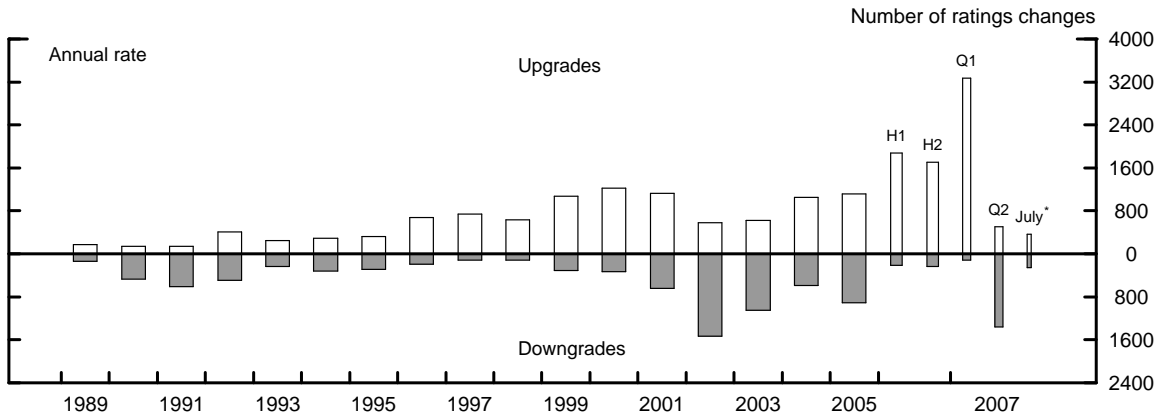
Gross Offerings of Municipal Securities

(Billions of dollars; monthly rate, not seasonally adjusted)

Type of security	2003	2004	2005	2006		2007		
				H1	H2	Q1	Q2	July ^p
Total	37.9	34.7	38.4	32.9	39.4	37.9	45.5	16.4
Long-term ¹	32.0	29.8	34.1	30.0	34.9	35.7	41.1	12.7
Refundings ²	10.0	10.8	15.6	9.7	11.4	17.7	14.8	1.7
New capital	22.1	19.0	18.6	20.3	23.4	18.0	26.3	11.1
Short-term	5.8	4.9	4.2	2.8	4.5	2.2	4.4	3.6
Memo: Long-term taxable	3.5	2.0	2.1	2.8	2.3	1.2	2.6	.2

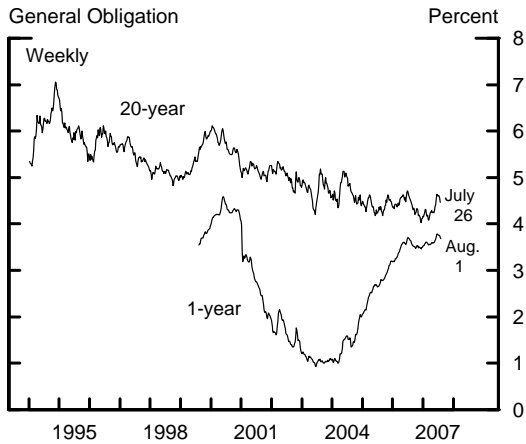
- 1. Includes issues for public and private purposes.
- 2. All issues that include any refunding bonds.
- p Based on preliminary data through July 26, 2007.

Ratings Changes



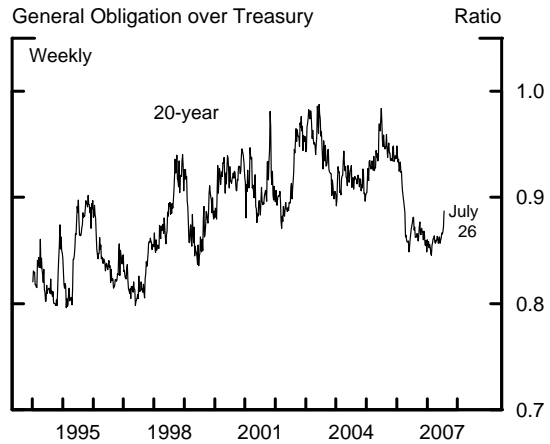
* Staff estimate based on data through July 25, 2007.
 Source: S&P's Credit Week Municipal and Ratings Direct.

Municipal Bond Yields



Source: Municipal Market Advisors and Bond Buyer.

Municipal Bond Yield Ratio



Source: Bond Buyer.

M2 Monetary Aggregate
(Based on seasonally adjusted data)

Aggregate and components	Percent change (annual rate) ¹					Level (billions of dollars), July (e)
	2005	2006	2007			
			Q1	Q2	July (e)	
M2	4.1	4.9	7.1	6.7	3.7	7,266
Components ²						
Currency	3.5	3.6	1.7	2.1	4.9	758
Liquid deposits ³	2.0	.8	6.6	7.0	.8	4,440
Small time deposits	18.9	18.6	4.5	4.2	-.5	1,176
Retail money market funds	-.2	13.0	18.9	13.1	22.6	885
Memo:						
Institutional money market funds	4.9	15.9	11.2	28.2	26.9	1,510
Monetary base	3.5	3.2	1.6	2.3	14.3	829

1. For years, Q4 to Q4; for quarters and months, calculated from corresponding average levels.

2. Nonbank traveler's checks are not listed.

3. Sum of demand deposits, other checkable deposits, and savings deposits.

e Estimated.

Commercial Bank Credit

(Percent change, annual rate, except as noted; seasonally adjusted)

Type of credit	2005	2006	Q1 2007	Q2 2007	July 2007 ^e	Level, ¹ July 2007 ^e
Total	10.5	9.6	8.6	9.4	9.1	8,339
<i>Loans²</i>						
Total	11.6	10.7	9.9	9.4	9.6	6,256
To businesses						
Commercial and industrial	13.5	16.4	7.9	11.0	19.1	1,256
Commercial real estate	17.0	13.6	10.3	11.4	3.6	1,521
To households						
Residential real estate	11.9	7.2	9.6	6.7	3.1	1,834
Revolving home equity	13.3	1.5	3.5	.1	5.5	459
Other	11.4	9.4	11.7	8.9	2.4	1,375
Consumer	3.1	5.2	7.5	5.2	14.4	769
Originated ³	.7	6.4	8.1	2.2	12.2	1,149
Other ⁴	8.5	11.0	14.8	12.8	16.1	876
<i>Securities</i>						
Total	7.5	6.3	4.8	9.6	7.5	2,083
Treasury and agency	.0	3.0	-2.1	-7.9	-2.8	1,151
Other ⁵	13.5	12.7	10.9	33.7	12.8	1,096

Note. Yearly annual rates are Q4 to Q4; quarterly and monthly annual rates use corresponding average levels. Data have been adjusted to remove the effects of mark-to-market accounting rules (FIN 39 and FAS 115), the consolidation of certain variable interest entities (FIN 46), the adoption of fair value accounting (FAS 159), and the effects of sizable thrift-to-bank and bank-to-thrift structure activity in October 2006 and March 2007 respectively. Data also account for breaks caused by reclassifications.

1. Billions of dollars. Pro rata averages of weekly (Wednesday) levels.

2. Excludes interbank loans.

3. Includes an estimate of outstanding loans securitized by commercial banks.

4. Includes security loans and loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.

5. Includes private mortgage-backed securities, securities of corporations, state and local governments, foreign governments, and any trading account assets that are not Treasury or agency securities, including revaluation gains on derivative contracts.

e Estimated.

Money and Bank Credit

M2 expanded at an annual rate of about 4 percent in July, down from its surprisingly strong pace earlier in the year. Liquid deposits and small time deposits, the main contributors to the slowdown, have been about flat in July, whereas retail money funds surged nearly 23 percent. Currency growth has been modest, held down by weak foreign demand.

Commercial bank credit is estimated to have grown at about a 9 percent rate in July, a pace just below that of the second quarter. Commercial and industrial loans continued to expand smartly. By contrast, lending to businesses through commercial real estate loans is estimated to have slowed notably in July. The weakness in residential real estate lending in June appears to have persisted last month, as banks sold a large volume of mortgages. According to the July Senior Loan Officer Opinion Survey, the demand for both nontraditional and subprime mortgages weakened further over the past three months. Consumer loan originations rebounded in July, although this increase was mainly a result of a thrift-to-bank consolidation within a bank holding company; without this boost, consumer loans continued to advance at a moderate pace.

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Appendix

Senior Loan Officer Opinion Survey on Bank Lending Practices

The July 2007 Senior Loan Officer Opinion Survey on Bank Lending Practices addressed changes in the supply of, and demand for, bank loans to businesses and households over the past three months.¹ Special questions in the survey asked banks about their involvement in, and assessment of, the outlook for the syndicated loan market. As in the April survey, banks were queried separately about changes in standards on, and demand for, prime, nontraditional, and subprime residential mortgages. This appendix is based on responses from fifty-two domestic banks and twenty foreign banking institutions.

Both domestic and foreign institutions indicated that they had eased terms on commercial and industrial (C&I) loans over the past three months, while a small net fraction of banks reported a tightening of standards on such loans over the same period. Respondents also noted in the July survey that they had tightened credit standards on commercial real estate loans. On net, domestic institutions reported somewhat weaker demand for C&I loans over the past three months. Branches and agencies of foreign institutions, in contrast, reportedly experienced moderately stronger demand for such loans, on net, over the same period. Both domestic and foreign institutions noted that the demand for commercial real estate loans has weakened, on net, since April.

With regard to loans to households, domestic institutions reported that lending standards on prime residential mortgages had tightened some, on balance, during the survey period, whereas considerable net fractions of respondents indicated that they had further tightened lending standards on nontraditional and subprime mortgage loans. Demand for prime and nontraditional residential mortgages was reportedly slightly weaker over the past three months, but a notable net fraction of banks reported that they had seen weaker demand for subprime residential mortgages over the same period. A significant net percentage of domestic banks also reported weaker demand for consumer loans over the past three months.

Business Lending

In the July survey, a small net fraction of domestic institutions reported that they had tightened lending standards on C&I loans to large and middle-market firms over the past three months. Domestic respondents, however, noted that they had further eased some terms on C&I loans to such firms over the same period. About 30 percent of respondents—a smaller net fraction than in the April survey—indicated that they had trimmed spreads of loan rates over their cost of funds over the previous three months, while smaller net fractions reported that they had reduced the costs of credit lines and eased loan covenants.

¹ The survey was conducted between July 16 and July 26. As a result, banks' responses are unlikely to reflect fully changes in their lending policies stemming from the recent volatility in financial markets.

Similarly, a very small net fraction of domestic institutions also reported having tightened lending standards on C&I loans to small firms in the July survey. About one-third of domestic banks, on net, reported that they had trimmed spreads of loan rates over their cost of funds for such borrowers over the past three months, and smaller net fractions reported that they had reduced the costs of credit lines and lowered premiums charged on riskier loans.

Fifteen percent of U.S. branches and agencies of foreign banks reported that they had tightened credit standards on C&I loans during the survey period. Regarding loan terms, a small net fraction of foreign institutions indicated that they had increased the maximum size of credit lines, whereas other terms on C&I loans at these institutions were reportedly little changed over the past three months.

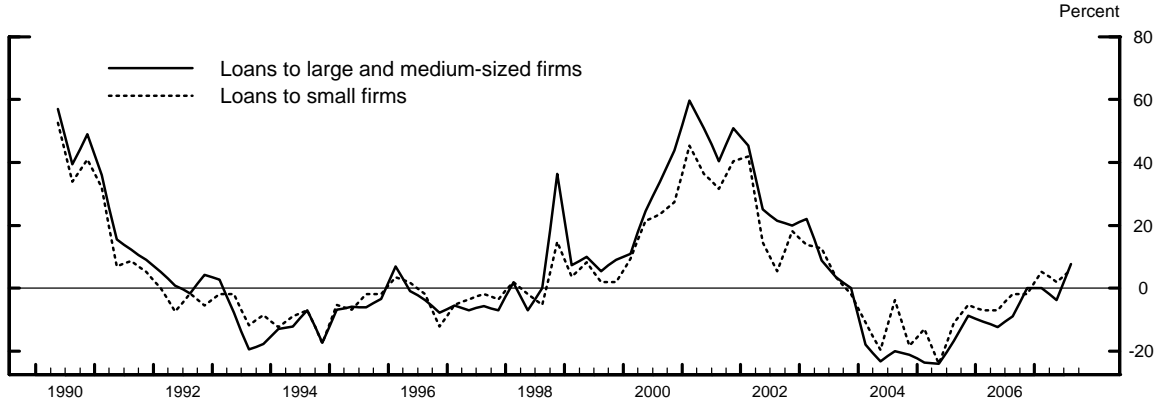
Nearly all domestic banks and all U.S. branches and agencies of foreign banks that reported having eased their lending standards and terms in the July survey pointed to more-aggressive competition from other banks or nonbank lenders as the most important reason for having done so. Institutions that reportedly moved to a more stringent lending posture, in contrast, cited a less favorable or more uncertain economic outlook, a reduced tolerance for risk, and decreased liquidity in the secondary market for C&I loans as the most important reasons for the change in their lending policies.

The net fraction of domestic banks reporting weaker demand for C&I loans in the survey period declined somewhat relative to the April survey. On net, about one-eighth of domestic banks noted that they had experienced weaker demand for C&I loans from large and middle-market, as well as from small firms in the July survey. In contrast, one-fifth of U.S. branches and agencies of foreign banks, on net, reported stronger demand for C&I loans over the past three months. The most frequently cited reasons for weaker demand at domestic banks were borrowers' decreased need to finance inventories and investment in plant and equipment. A relatively large number of domestic and foreign institutions that reported an increase in demand for C&I loans, pointed to greater financing needs for merger and acquisition (M&A) activity as the most important reason for the rise.

Regarding future business, about 13 percent of domestic respondents, on net, reported that the number of inquiries from potential business borrowers had decreased over the previous three months, about the same percentage as in the April survey. On net, foreign respondents indicated that the number of inquiries from potential business borrowers was unchanged over the past three months.

Measures of Supply and Demand for C&I Loans, by Size of Firm Seeking Loan

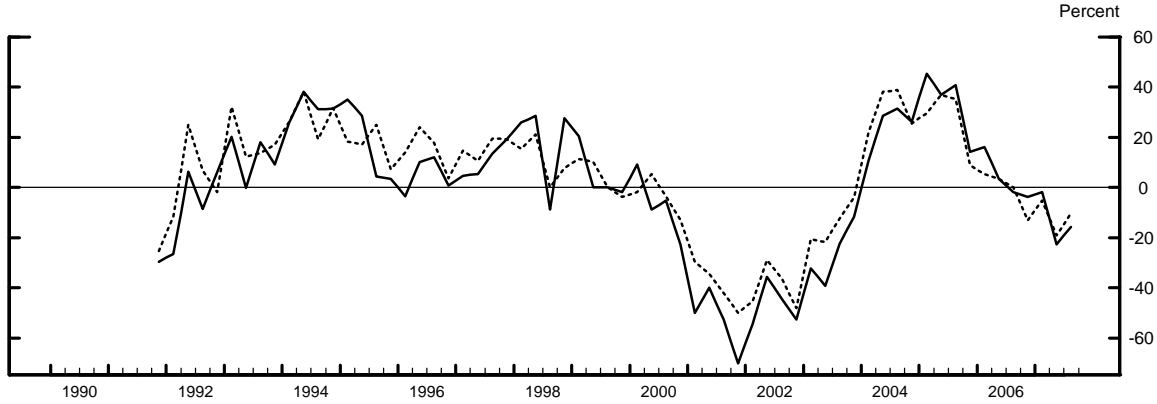
Net Percentage of Domestic Respondents Tightening Standards for C&I Loans



Net Percentage of Domestic Respondents Increasing Spreads of Loan Rates over Banks' Costs of Funds



Net Percentage of Domestic Respondents Reporting Stronger Demand for C&I Loans



The July survey included a set of special questions regarding banks' involvement in, and assessment of the outlook for, the syndicated loan market.² In general, syndicated loans accounted for a relatively small fraction of C&I loans on domestic banks' books, but the share was substantial for some banks. About one-fourth of domestic institutions noted that syndicated loans accounted for less than 5 percent of their bank's C&I loans, and about one-half reported that syndicated loans accounted for between 5 percent and 20 percent of their C&I loan portfolios.³ About one-fifth of respondents noted that syndicated loans accounted for between 21 percent and 50 percent of their C&I loans. Four domestic respondents noted that these loans accounted for more than 50 percent—but less than 75 percent—of C&I loans on their books. These institutions accounted for about 10 percent of all C&I loans on the books of the domestic banks that responded to this special question. In general, the share of syndicated loans did not appear to be related to the size of banks' portfolios of C&I loans. At foreign institutions, syndicated loans accounted for a more significant fraction of C&I loans on respondents' books: Of the twenty respondents, four foreign institutions reported that syndicated loans accounted for between 35 percent and 50 percent of their C&I loan portfolios, whereas six institutions reported that such loans accounted for between 50 percent and 75 percent of C&I loans. Finally, nine foreign banks reported that syndicated loans accounted for more than 75 percent of C&I loans on their books. One relatively small foreign respondent noted that syndicated loans accounted for between 5 percent and 20 percent of its C&I loans. As was the case for domestic institutions, the share of syndicated loans did not appear to be related to the size of the foreign banks' loan portfolios.

According to the July survey, leveraged syndicated loans generally accounted for a relatively modest fraction of all syndicated loans on the books of most domestic and foreign institutions.⁴ About one-half of domestic banks reported that leveraged syndicated credits accounted for less than 5 percent of syndicated loans on their books, whereas approximately 40 percent noted that such loans accounted for between 5 percent and 35 percent of their syndicated loans. About one-tenth of domestic respondents reported that leveraged loans accounted for more than 35 percent—but less than 75 percent—of their syndicated loans. Regarding foreign banks, about one-third of

² A few large banks with prominent position in the syndicated loan market have not yet provided responses to these special questions. We expect to have their responses in time for the public release of the survey results. The number of domestic banks that responded to these special questions varied from forty-four to forty-nine depending on the question. According to Call Reports, these respondents accounted for between 43 percent and 53 percent of all C&I loans on the books of domestic commercial banks as of March 31, 2007. The number of foreign institutions that responded to these special questions varied from eighteen to twenty depending on the question. As of March 31, 2007, the foreign respondents accounted for about 55 percent of all C&I loans on the books of U.S. branches and agencies of foreign banks.

³ Three relatively small banks reported that they do not hold any syndicated loans.

⁴ In the survey, a loan was defined as leveraged if the obligor's postfinancing leverage—as measured by ratios of debt to assets, debt to equity, or cash flow to total debt or by other such standards unique to particular industries—significantly exceeded industry norms for leverage.

these institutions reported that leveraged loans accounted for more than 20 percent—but less than 50 percent—of the syndicated loans on their books. About the same fractions of foreign banks noted that leveraged loans accounted for between 5 percent and 20 percent and for less than 5 percent of syndicated loans on their books.

Domestic institutions reported that loans originated to fund leveraged buyout (LBO) activity typically accounted for a relatively small fraction of syndicated loans on their books. About two-thirds of domestic respondents noted that LBO-related loans accounted for less than 5 percent of syndicated loans on their books, whereas about 30 percent reported that such loans accounted for between 5 percent and 35 percent of their syndicated loans. Finally, about 6 percent of respondents noted that LBO-related loans accounted for more than 35 percent—but less than 75 percent—of syndicated loans on their books. Foreign institutions also mostly reported relatively small exposure to LBO-related loans. About 65 percent of foreign respondents reported that LBO-related loans accounted for less than 5 percent of their syndicated loans, and about one-fifth of respondents noted that such loans accounted for between 5 percent and 35 percent of their syndicated loans. Only three foreign institutions reported that LBO-related loans accounted for more than 35 percent—but less than 75 percent—of their syndicated loan portfolios.

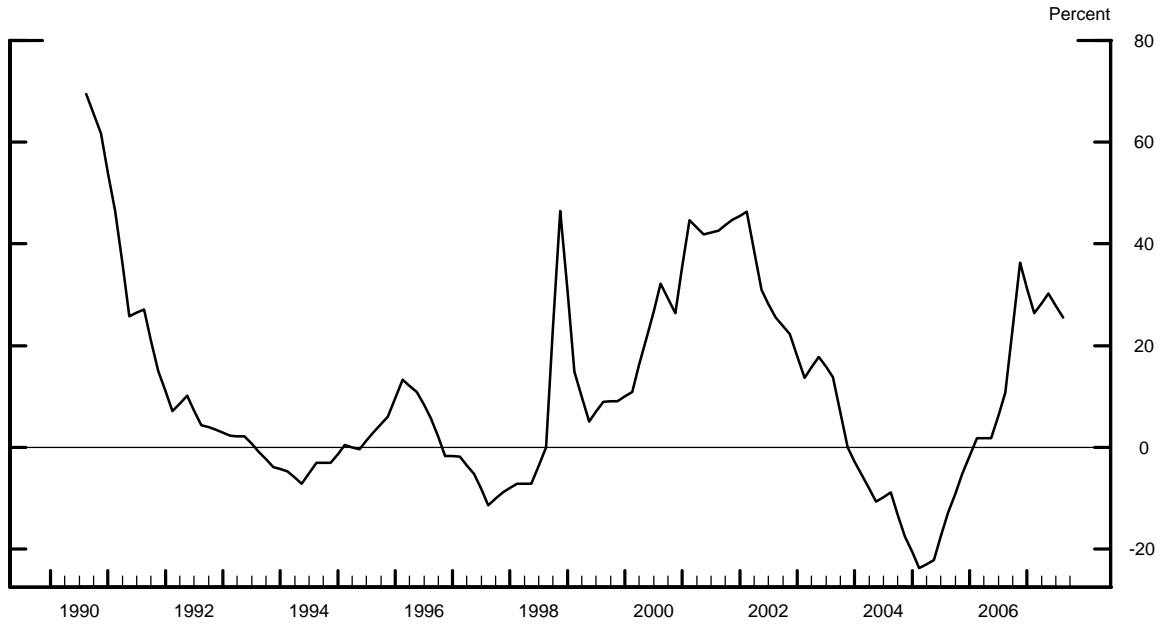
At both domestic and foreign institutions, bridge loans and equity bridge loans generally accounted for very small fractions of syndicated loans.⁵ About one-half of domestic institutions reported that they did not have any bridge loans on their books, and about 45 percent of domestic banks noted that such loans accounted for between 0 percent and 5 percent of their syndicated loans. Only one institution reported that bridge loans accounted for between 5 percent and 20 percent of its syndicated loan portfolio. Regarding equity bridge loans, three-fourths of domestic respondents reported that they did not have any such loans on their books, and the remaining fraction noted that equity bridge loans accounted for between 0 percent and 5 percent of their syndicated loans. Of the nineteen foreign respondents, five banks indicated that they did not have any bridge loans on their books, whereas twelve banks noted that bridge loans accounted for between 0 percent and 5 percent of their syndicated loans. Only two foreign institutions reported that bridge loans accounted for between 5 percent and 20 percent of their syndicated loans. Regarding equity bridge loans, two-thirds of foreign institutions reported that they did not have any such loans on their books, whereas the remaining banks noted that such loans accounted for between 0 percent and 5 percent of their syndicated loans.

Domestic and foreign banks reportedly expect a tightening of credit standards and terms in the syndicated loan market in coming months, in part because of a very large number of deals in the

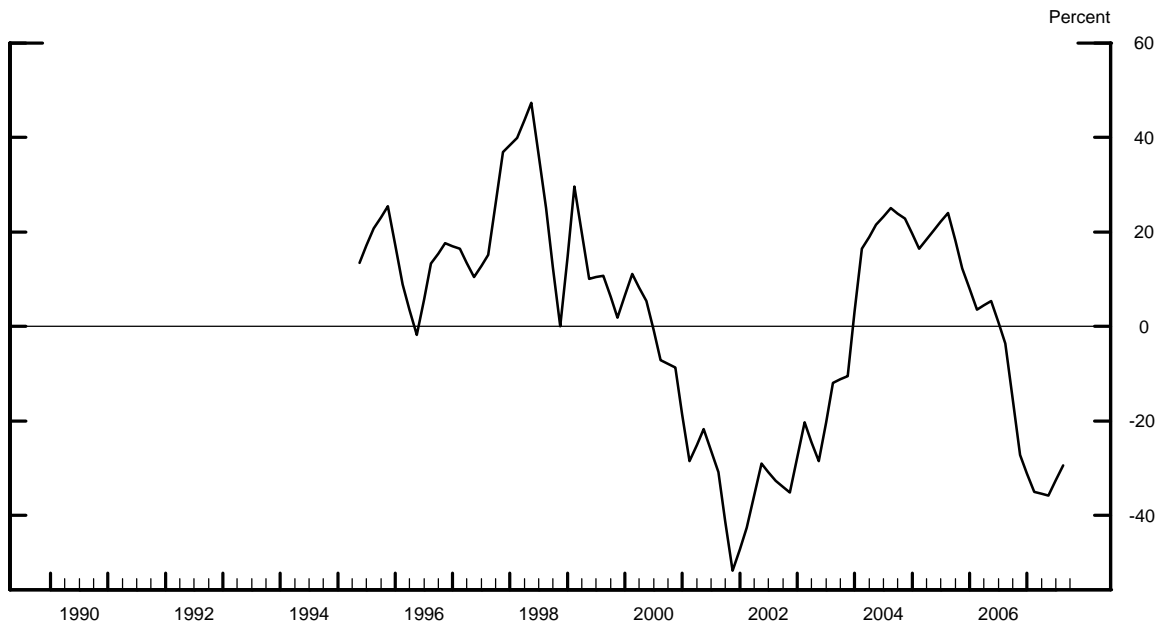
⁵ In the survey, bridge loans were defined as M&A-related loans that banks expected to be paid down with funds raised in capital markets within the next twelve months. Equity bridge loans were defined as loans that are originated to LBO sponsors to provide financing applied toward the sponsors' equity contributions in buyouts and that are subsequently paid down with funds raised in equity sales.

Measures of Supply and Demand for Commercial Real Estate Loans

Net Percentage of Domestic Respondents Tightening Standards for Commercial Real Estate Loans

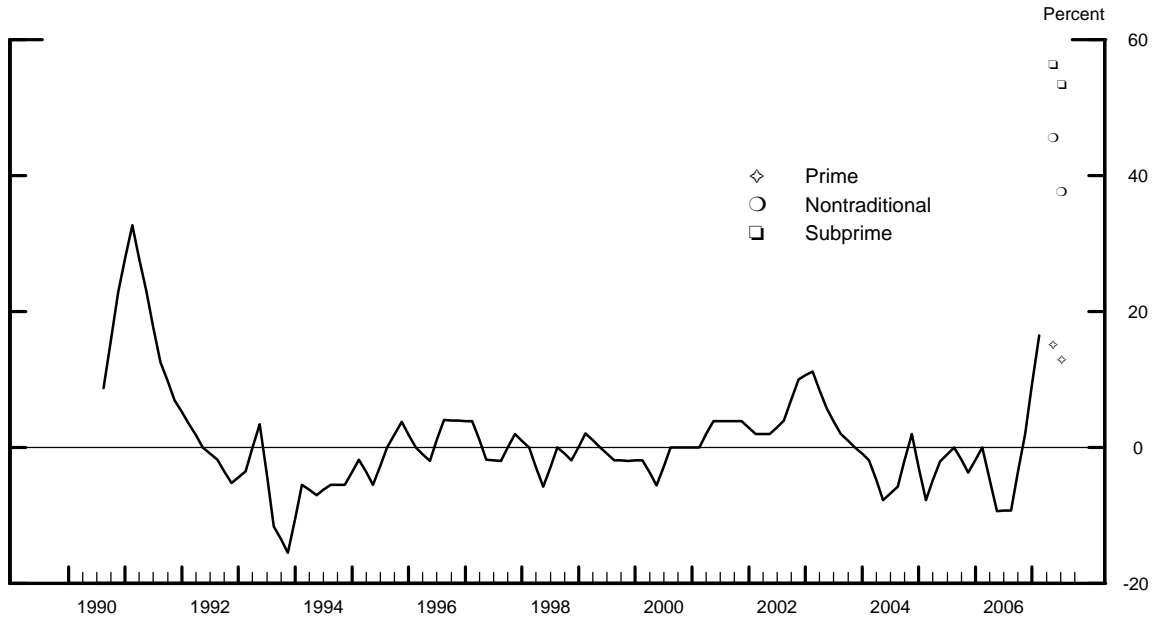


Net Percentage of Domestic Respondents Reporting Stronger Demand for Commercial Real Estate Loans



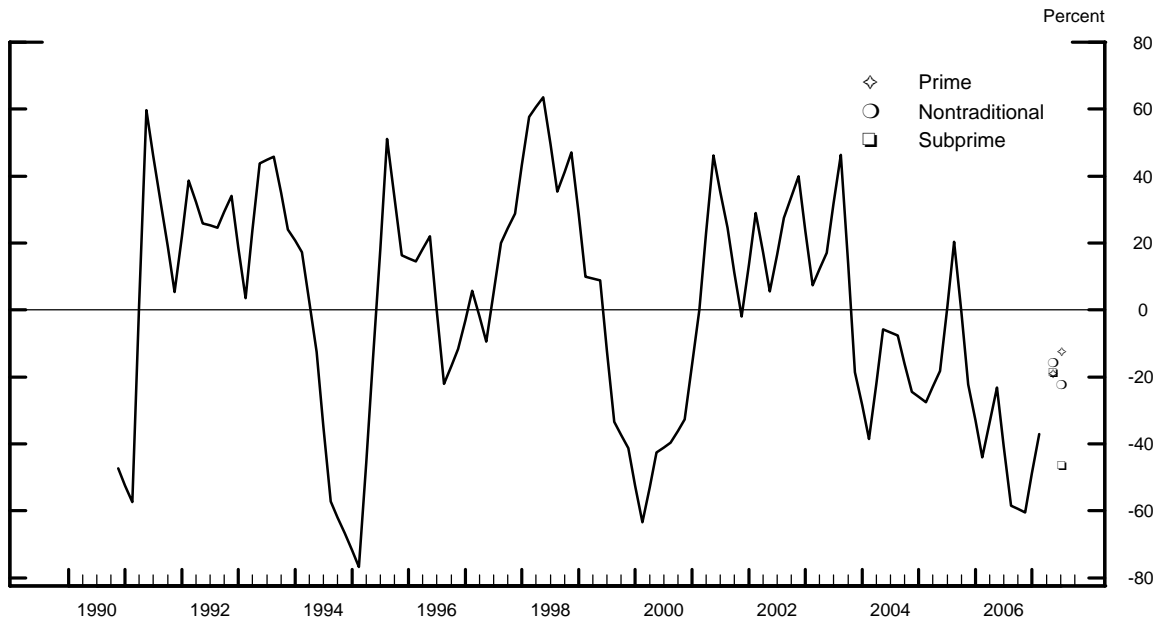
Measures of Supply and Demand for Residential Mortgage Loans

Net Percentage of Domestic Respondents Tightening Standards for Mortgage Loans



Note: Starting in 2007:Q2, changes in standards for prime, nontraditional, and subprime mortgage loans are reported separately.

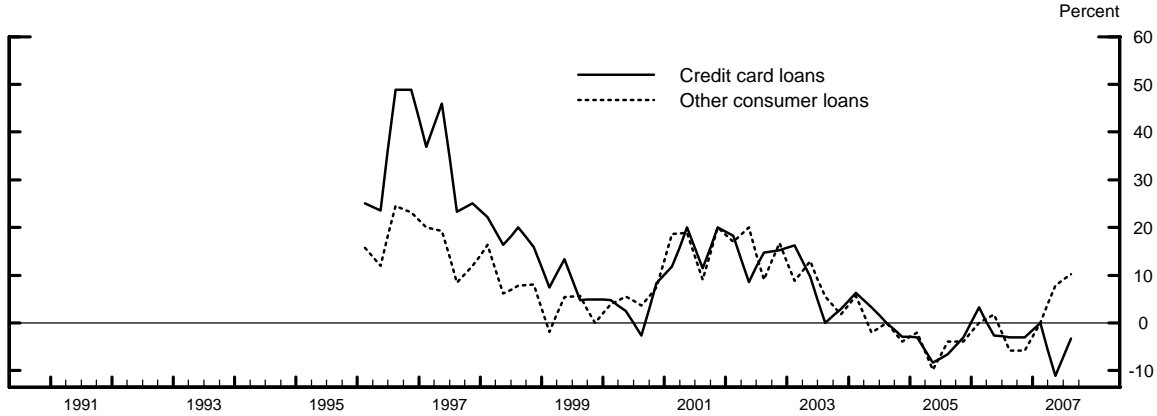
Net Percentage of Domestic Respondents Reporting Stronger Demand for Mortgage Loans



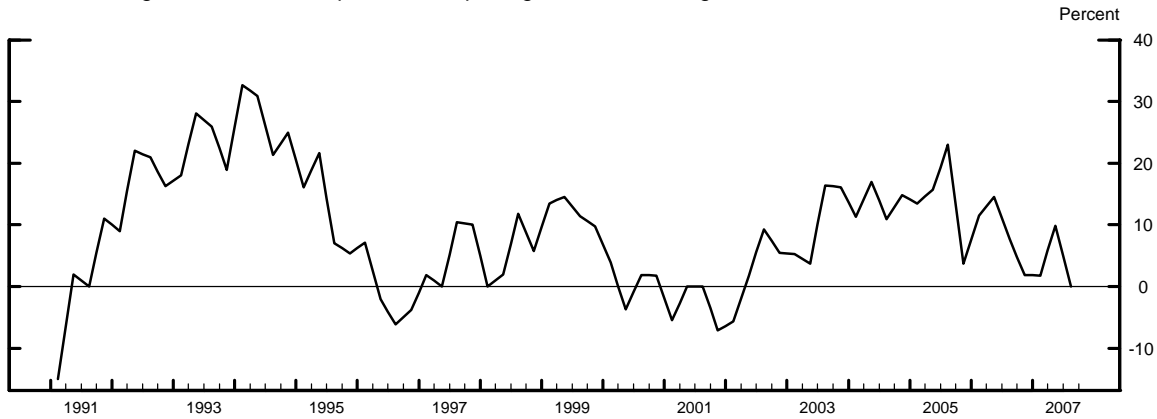
Note: Starting in 2007:Q2, changes in demand for prime, nontraditional, and subprime mortgage loans are reported separately.

Measures of Supply and Demand for Consumer Loans

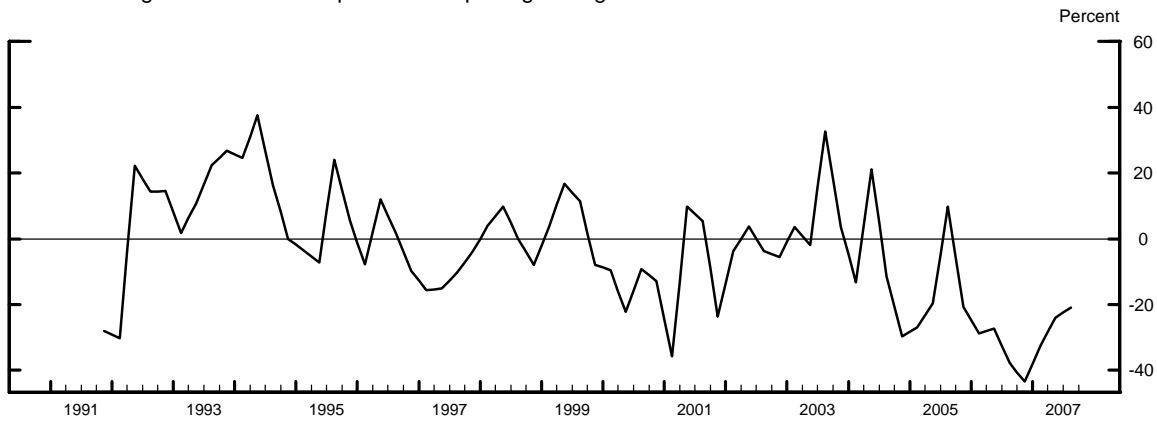
Net Percentage of Domestic Respondents Tightening Standards for Consumer Loans



Net Percentage of Domestic Respondents Reporting Increased Willingness to Make Consumer Installment Loans



Net Percentage of Domestic Respondents Reporting Stronger Demand for Consumer Loans



pipeline. Indeed, about two-thirds of domestic respondents and almost all foreign respondents expect tighter lending standards, a widening of loan spreads, an increased number of covenants, and more-stringent covenants. Moreover, more than one-third of domestic respondents and approximately two-thirds of foreign respondents expect a reduction in the loan portion of financing deals and the introduction of call protection or original issue discounts on loan deals.

Lending standards for commercial real estate loans were reportedly tightened further over the survey period: About one-fourth of domestic institutions—a slightly smaller net fraction than in the previous survey—and about one-third of foreign institutions indicated that they had tightened lending standards on commercial real estate loans over the past three months. Regarding demand, approximately one-fourth of domestic and foreign institutions reported that demand for commercial real estate loans had weakened over the past three months.

Household Lending

As in the April survey, banks were asked to report separately about changes in standards on, and demand for, prime, nontraditional, and subprime residential mortgages. In the July survey, banks indicated that they had tightened their lending standards on the three mortgage loan categories over the past three months, although the net fractions of banks that reported doing so were somewhat smaller than in the April survey. About 13 percent of domestic banks reportedly tightened their lending standards on prime residential mortgages over the past three months.⁶ By contrast, about 38 percent of respondents—out of the forty institutions that originated nontraditional residential mortgages—noted that they had tightened standards on these types of mortgage products.⁷ Moreover, of the fifteen institutions that reported having originated subprime residential mortgages, about 53 percent reported that they had tightened standards on such loans.⁸

As in the April survey, tighter standards on subprime and nontraditional mortgage loans were not necessarily associated with more-stringent lending policies on prime loans. Indeed, of the eight institutions that reported having tightened standards on subprime residential mortgages over the past three months, only one bank had tightened standards on prime residential mortgages. Of the fifteen domestic banks that tightened standards on nontraditional mortgage loans, five tightened standards on prime mortgages.

⁶ Forty-seven institutions reported that they had originated prime residential mortgages. These forty-seven banks accounted for about 60 percent of residential real estate loans on the books of all commercial banks as of March 31, 2007.

⁷ These forty institutions accounted for about 51 percent of residential real estate loans on the books of all commercial banks as of March 31, 2007.

⁸ These fifteen institutions accounted for about 47 percent of residential real estate loans on the books of all commercial banks as of March 31, 2007.

On net, about one-tenth of domestic banks—a smaller net fraction than in the April survey—reported weaker demand for prime mortgage loans, and about one-fifth of respondents—about the same net fraction as in the April survey—experienced weaker demand for nontraditional mortgage loans. In contrast, about 46 percent of respondents, on net—more than twice the percentage in the April survey—reported weaker demand for subprime residential mortgages over the past three months.

On balance, domestic respondents' willingness to make consumer installment loans and their lending standards for approving applications on credit card loans were little changed over the past three months. A small net fraction of banks reported having tightened lending standards on non-credit-card consumer loans over the same period. Some terms on both categories of consumer loans were tightened a touch during the survey period. On net, about one-eighth of respondents reported having raised spreads of interest rates charged on outstanding credit card balances relative to their cost of funds, and about one-fifth of respondents reported having reduced the extent to which consumer loans other than credit card loans were granted to customers who did not meet credit-scoring thresholds. The remaining terms on both types of consumer loans were reportedly little changed. Finally, on net, about one-fifth of domestic respondents reported that they had experienced weaker demand for consumer loans, about the same net fraction as in the April survey.

International Developments

International Developments

U.S. International Transactions

Trade in Goods and Services

The U.S. international trade deficit widened to \$60 billion in May from \$58.7 billion in April (revised). The widening of the deficit reflected both higher exports and imports, but with imports increasing more than exports.

Trade in Goods and Services

	2006	Annual rate			Monthly rate		
		2006	2007		2007		
		Q4	Q1	Q2 ^e	Mar.	Apr.	May
Percent change							
<i>Nominal BOP</i>							
Exports	13.3	13.5	5.7	9.6	2.6	-.1	2.2
Imports	4.7	-7.3	3.8	7.4	4.4	-2.0	2.3
<i>Real NIPA</i>							
Exports	9.3	14.3	1.1	6.4	...	...	...
Imports	3.7	1.6	3.9	-2.6	...	...	...
Billions of dollars							
<i>Nominal BOP</i>							
Net exports	-758.5	-707.7	-707.2	-712.2	-62.4	-58.7	-60.0
Goods, net	-838.3	-801.4	-803.5	-818.1	-70.7	-67.3	-69.0
Services, net	79.7	93.6	96.3	105.8	8.4	8.7	9.0

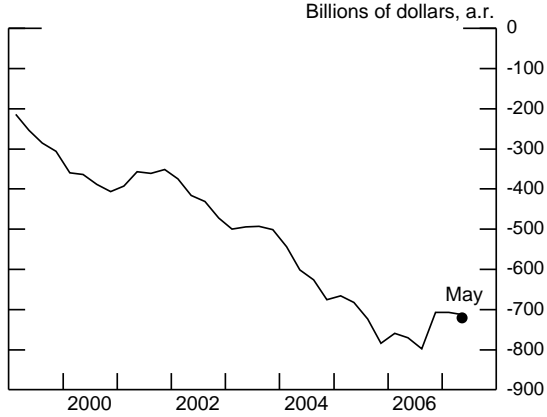
e. BOP data are two months at an annual rate; NIPA data are BEA's advance estimate.
Source. U.S. Department of Commerce, Bureaus of Economic Analysis and Census.
n.a. Not available. ... Not applicable.

In May, the value of exports of goods and services increased 2.2 percent, following little change in April. The May increase mostly reflected a 3.3 percent jump in exports of nonagricultural goods (excluding gold), although exports of services also rose. Within goods, exports of capital goods moved up briskly, rising 5.5 percent; the increase was led by a particularly large jump in exports of aircraft but was also supported by higher exports of computers and semiconductors. Exports of industrial supplies exhibited strong growth, boosted by a jump in exports of petroleum products. After a sharp 10.6 percent increase in April, agricultural exports edged down in May. For the second consecutive month, automotive exports declined modestly.

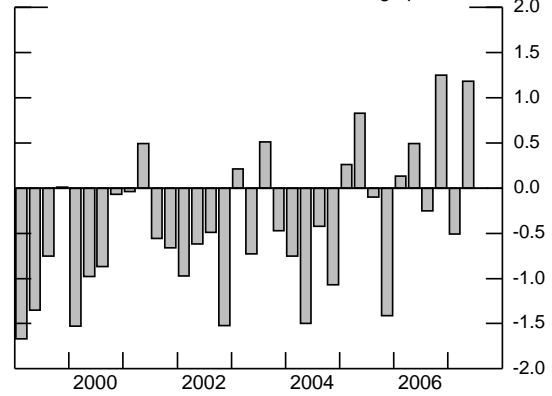
The average value of exports in April and May increased 9.6 percent (a.r.) from the first quarter. Exports of agricultural goods and industrial supplies exhibited particular strength. In contrast, exports of capital goods edged down, reflecting declines in exports of aircraft and computers. In the advance NIPA release, real exports of goods and services rose at an annual rate of 6.4 percent in the second quarter.

U.S. International Trade in Goods and Services (Quarterly)

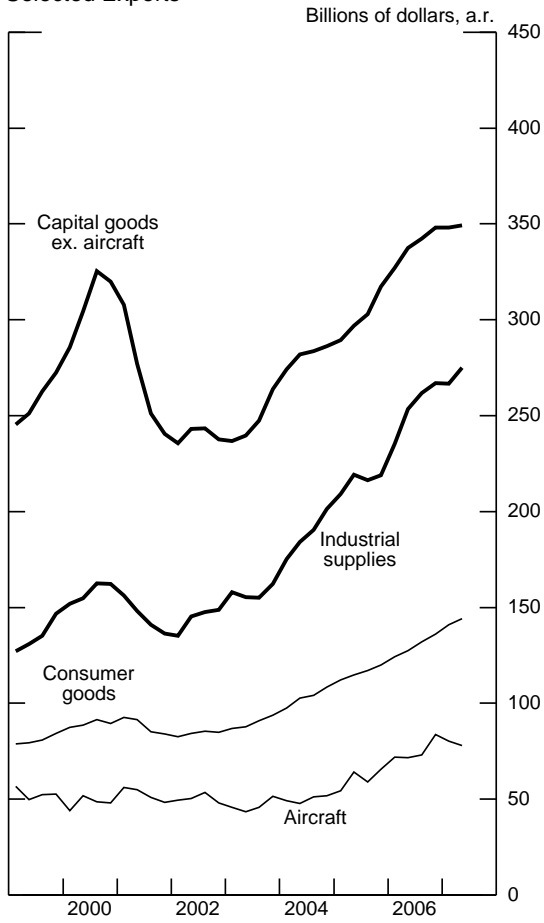
Trade Balance



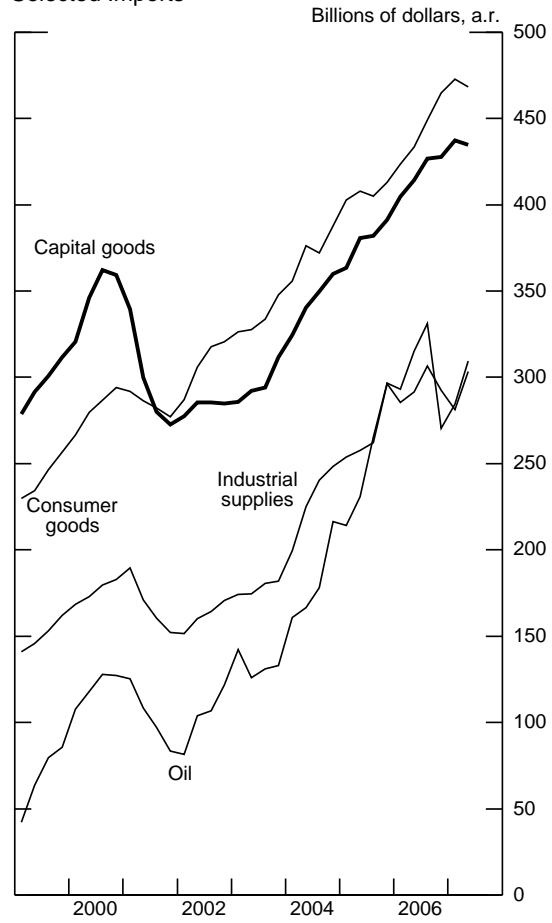
Contribution of Net Exports to Real GDP Growth



Selected Exports



Selected Imports



U.S. Exports and Imports of Goods and Services
(Billions of dollars, a.r., BOP basis)

	Levels				Change ¹			
	2007		2007		2007		2007	
	Q1	Q2 ^e	Apr.	May	Q1	Q2 ^e	Apr.	May
Exports of G&S	1531.7	1567.2	1550.0	1584.4	21.2	35.5	-.9	34.4
Goods exports	1080.5	1105.4	1091.2	1119.6	14.5	24.9	-1.5	28.4
Gold	10.6	15.9	17.8	13.9	1.6	5.3	.8	-4.0
Other goods	1069.9	1089.5	1073.4	1105.7	13.0	19.6	-2.3	32.4
Capital goods	428.1	427.0	415.5	438.5	-3.6	-1.1	-7.5	23.0
Aircraft & parts	80.4	77.9	71.9	83.8	-3.3	-2.5	-1.1	11.8
Computers & accessories	45.3	41.5	40.5	42.5	-2.6	-3.8	-.9	2.0
Semiconductors	50.2	48.7	47.9	49.4	-.6	-1.5	-2.5	1.5
Other capital goods	252.2	258.9	255.1	262.7	2.9	6.7	-3.0	7.6
Automotive	111.5	117.7	117.9	117.4	2.0	6.1	-.8	-.4
Ind. supplies (ex. ag., gold)	266.7	274.8	269.7	280.0	-.3	8.1	1.2	10.3
Consumer goods	140.9	144.0	143.6	144.4	4.9	3.2	1.7	.8
Agricultural	79.3	86.2	86.4	86.1	3.9	6.9	8.3	-.3
All other goods	43.4	39.9	40.3	39.4	6.0	-3.5	-2.0	-1.0
Services exports	451.2	461.8	458.8	464.8	6.7	10.6	.6	6.0
Imports of G&S	2238.8	2279.4	2254.0	2304.8	20.6	40.6	-45.5	50.8
Goods imports	1883.9	1923.5	1899.3	1947.6	16.6	39.5	-42.2	48.3
Oil	283.4	309.4	300.0	318.7	13.1	26.0	.5	18.7
Gold	7.8	11.8	12.7	11.0	2.7	4.0	-2.5	-1.6
Other goods	1592.7	1602.3	1586.7	1617.8	.9	9.6	-40.3	31.2
Capital goods	437.4	434.6	428.4	440.9	9.7	-2.8	-5.9	12.5
Aircraft & parts	32.8	32.6	33.0	32.3	2.2	-.1	-.8	-.7
Computers & accessories	108.5	102.1	101.8	102.4	6.6	-6.4	-1.4	.6
Semiconductors	27.0	26.2	26.3	26.2	-.2	-.8	.0	-.1
Other capital goods	269.2	273.6	267.3	279.9	1.2	4.4	-3.8	12.6
Automotive	253.4	249.9	252.9	246.8	-7.2	-3.6	-12.6	-6.1
Ind. supplies (ex. oil, gold)	281.2	303.1	297.3	309.0	-11.1	21.9	5.2	11.7
Consumer goods	473.0	468.4	464.9	471.8	8.2	-4.6	-20.0	6.9
Foods, feeds, bev.	80.1	80.2	79.1	81.4	3.2	.1	-3.0	2.3
All other goods	67.5	66.1	64.1	68.0	-2.0	-1.4	-3.9	3.9
Services imports	354.9	356.0	354.7	357.2	4.0	1.0	-3.3	2.6
<i>Memo:</i>								
Oil quantity (mb/d)	14.32	13.48	13.42	13.55	1.01	-.80	-1.12	.14
Oil import price (\$/bbl)	54.33	62.81	61.22	64.39	-1.29	8.52	4.84	3.17

1. Change from previous quarter or month. e. Average of two months.

Source. U.S. Department of Commerce, Bureaus of Economic Analysis and Census.

The value of imported goods and services rose 2.3 percent in May following a 2 percent decline in April. About half of the May increase was due to non-oil goods, but oil and services imports were also higher. The rise in imports of non-oil goods was led by imports of non-oil industrial supplies and capital goods, which increased 3.9 and 2.9 percent, respectively. After a decline of 4.7 percent in April, imports of automotive products fell a further 2.4 percent in May.

The average value of imports in April and May rose 7.4 percent (a.r.) from the first quarter. The increase partly reflected a large rise in the value of imported oil, as a jump in the price of imported oil more than offset a decline in quantity. Imports of non-oil industrial supplies also rose sharply. Imports of services increased only slightly, whereas imports of autos, consumer goods, and capital goods all declined. In the advance NIPA release, real imports of goods and services fell 2.6 percent in the second quarter.

Prices of Internationally Traded Goods

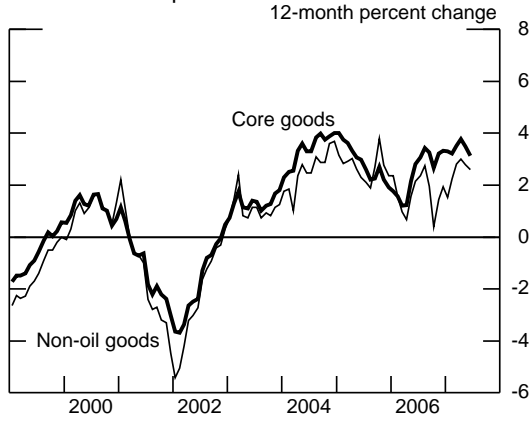
Non-oil imports. In June, prices of U.S. imports of core goods rose 0.2 percent, below the 0.5 percent increase in May. Prices for imported material-intensive goods rose 0.5 percent, more slowly than in recent months, but they still accounted for the bulk of the increase in core prices. Within material-intensive goods, non-fuel industrial supplies led the way, as prices for imported metals jumped in June. Prices for imported finished goods inched up in June, as the boost from a sizable jump in prices for capital goods (excluding computers and semiconductors) was offset by flat prices for consumer goods and a sluggish increase in prices for automobiles. Outside of core imports, the price for imported natural gas rose 0.5 percent, prices for imported semiconductors were unchanged, and prices for imported computers fell.

In the second quarter, core import prices rose about 3½ percent at an annual rate (on a NIPA basis), continuing the acceleration from the first quarter. Prices for material-intensive goods were up 12 percent (a.r.), whereas prices for finished goods increased 1¼ percent (a.r.). Within material-intensive goods, prices for agricultural products and metals both rose sharply, while most of the price increase for imported finished goods reflects higher prices for capital goods (excluding computers and semiconductors).

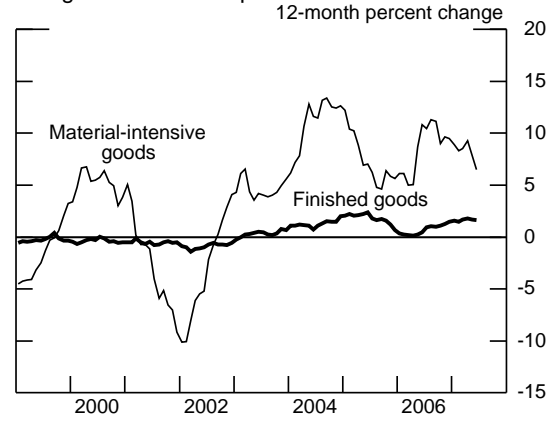
Oil. The BLS price index of imported oil rose 4.7 percent in June. The index has risen for five consecutive months and stands 28 percent above its level in January. The spot price of West Texas Intermediate (WTI) crude oil increased roughly 6 percent in June and nearly 8 percent in July. In July, the spot price averaged around \$74 per barrel.

Prices of U.S. Imports and Exports

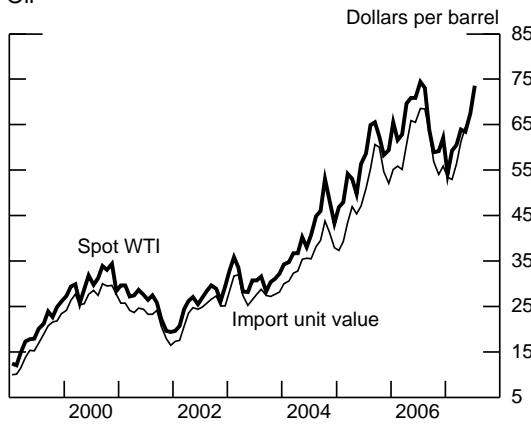
Merchandise Imports



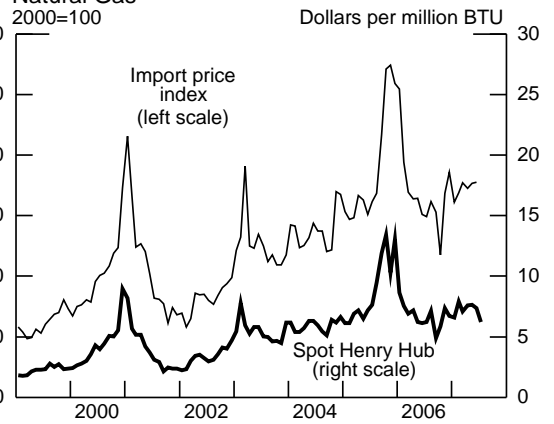
Categories of Core Imports



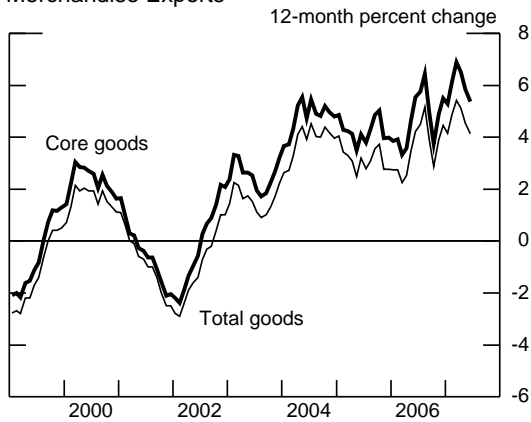
Oil



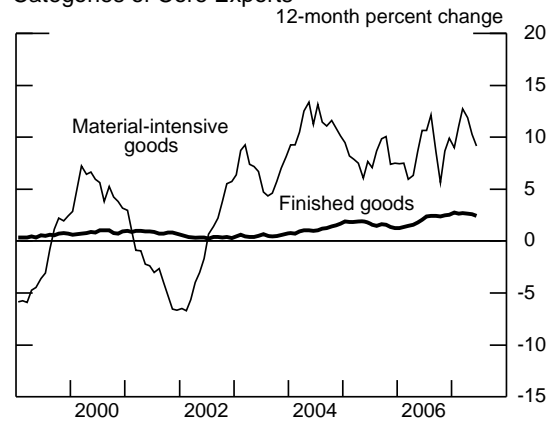
Natural Gas



Merchandise Exports



Categories of Core Exports



Prices of U.S. Imports and Exports
(Percentage change from previous period)

	Annual rate			Monthly rate		
	2006	2007		2007		
	Q4	Q1	Q2	Apr.	May	June
	----- BLS prices -----					
Merchandise imports	-11.9	1.8	15.5	1.4	1.1	1.0
Oil	-51.9	-3.2	93.8	6.8	3.7	4.7
Non-oil	1.8	2.6	3.4	.3	.5	.2
Core goods ¹	1.9	3.4	4.4	.5	.5	.2
Finished goods	1.2	1.8	1.3	.1	.1	.1
Cap. goods ex. comp. & semi.	1.2	3.1	3.1	.3	.3	.5
Automotive products	.8	.3	.9	.1	.1	.1
Consumer goods	1.5	1.9	.3	.0	.0	.0
Material-intensive goods	3.6	6.4	12.0	1.3	1.5	.5
Foods, feeds, beverages	6.5	9.8	8.2	1.4	.9	.2
Industrial supplies ex. fuels	1.8	3.8	13.0	1.2	1.7	.5
Computers	-2.5	-9.5	-8.3	-.7	-.5	-.2
Semiconductors	2.2	-6.8	-20.8	-4.1	-1.4	.0
Natural gas	7.6	33.6	16.1	-2.5	2.2	.5
Merchandise exports	.4	7.2	5.7	.4	.2	.3
Core goods ²	.8	9.3	7.2	.5	.2	.4
Finished goods	1.9	3.6	2.3	.3	.2	.0
Cap. goods ex. comp. & semi.	3.0	4.4	2.4	.3	.2	.0
Automotive products	.9	1.7	.9	.1	.0	.1
Consumer goods	.3	3.4	3.1	.6	.3	.0
Material-intensive goods	-.7	17.0	13.6	.8	.3	.9
Agricultural products	20.9	27.8	7.6	-1.4	.1	2.9
Industrial supplies ex. ag.	-5.7	14.1	15.2	1.3	.5	.3
Computers	-3.4	-12.8	-12.1	-1.9	-.3	-.3
Semiconductors	-3.3	-.8	3.8	.7	.0	.0
	----- NIPA prices -----					
Chain price index						
Imports of goods & services	-9.4	1.0	12.2	...	...	...
Non-oil merchandise	1.2	2.1	2.5	...	...	...
Core goods ¹	1.3	2.7	3.6	...	...	...
Exports of goods & services	-.8	3.6	4.9	...	...	...
Total merchandise	.1	3.5	4.7	...	...	...
Core goods ²	.3	6.0	7.0	...	...	...

1. Excludes computers, semiconductors, and natural gas.

2. Excludes computers and semiconductors.

n.a. Not available. ... Not applicable.

The rise in oil prices over the past two months appears to reflect recent supply disruptions and concerns of a tighter oil market going forward. Planned and unplanned production outages in the North Sea, worsening violence in Nigeria, and continued OPEC production restraint have provided upward support for oil prices. In addition, global oil demand has remained robust. Moreover, the idiosyncratic weakness that has recently characterized the spot price of WTI relative to the prices of other grades of oil has begun to dissipate as inventories at Cushing, Oklahoma, the delivery point for WTI, have run off from record levels.

Exports. Prices of U.S. exports of core goods rose 0.4 percent in June, somewhat faster than in May. All of the increase came from material-intensive goods; prices of exported finished goods were flat in June. Within material-intensive goods, prices of exported agricultural products rose almost 3 percent in June, after falling in April and being roughly flat in May, with prices for imported grains and meat both soaring in the month. Prices of exported computers fell 0.3 percent in June, a modest decline compared to the average decline over the past year, and prices for exported semiconductors were unchanged for the second consecutive month.

In the second quarter, core export prices rose 7 percent at an annual rate (on a NIPA basis), about 1 percentage point faster than in the first quarter. The step up in inflation is attributable to prices for nonagricultural industrial supplies. There was a sharp deceleration in prices for agricultural exports, which rose at an annual rate of 7½ percent after rising at an average rate of over 20 percent in the three previous quarters.

U.S. International Financial Transactions

Total net foreign private purchases of U.S. long-term securities (line 4 of the Summary of U.S. International Transactions table) totaled \$125 billion in May, the first month during which total foreign private net purchases have exceeded \$100 billion, but moderated in June to \$62 billion. May's inflows were led by record foreign net purchases of both U.S. corporate debt (line 4c) and U.S. equities (line 4d). Foreign acquisitions of U.S. corporate debt dropped to an unusually low \$16 billion in June. Foreign acquisitions of U.S. equities also fell in June, but remained strong at \$27 billion. Private net purchases of Treasuries (line 4a) were relatively robust in both May and June following large net sales in April. There were small net purchases of agency debt securities in both May and June.

For the second quarter as a whole, total private inflows were exceptionally large at \$222 billion (line 4), resulting primarily from record inflows into U.S. equities (\$105 billion). Foreign investors purchased more U.S. equities in the second quarter of 2007 than they did in all of 2005 and are on pace to double their acquisitions of 2006. Foreign purchases of U.S. corporate debt (\$100 billion) accounted for the bulk of the remaining inflows into U.S. securities during the quarter and were in line with inflows seen in recent quarters. There were modest net purchases of agency debt securities and small net sales of Treasuries during the quarter.

Foreign official flows in May and June (line 1) followed a markedly different pattern from private flows, with very small inflows recorded in May (\$8 billion) and very large inflows recorded in June (\$58 billion).

. For the quarter, total official inflows were measured at \$100 billion, a bit lower than the average of recent quarters.

U.S. residents' acquisitions of foreign securities (line 5) in May and June were in keeping with recent trends and were evenly distributed between equity and debt securities. Outflows during the second quarter (\$88 billion) were about the same as those recorded in the first quarter and a bit ahead of last year's pace. Most of these acquisitions were recorded versus the United Kingdom, which yields little conclusive information as to the ultimate destination of these flows as many non-U.K. securities trade on U.K. exchanges.

The normally volatile banking sector (line 3) posted a small net inflow during the quarter despite a large net outflow in June.

Combining official flows with private banking and private security flows yields a net inflow in the second quarter of \$241 billion, roughly \$40 billion above the first quarter's figure for this measure.

Summary of U.S. International Transactions
(Billions of dollars, not seasonally adjusted except as noted)

	2005	2006	2006		2007			
			Q3	Q4	Q1	Q2	May	Jun
Official financial flows	272.3	444.9	110.0	86.3	145.8	100.4	8.0	58.1
1. Change in foreign official assets in the U.S. (increase, +)	258.2	442.5	109.0	84.9	145.8	100.3	8.1	58.2
a. G-10 countries + ECB	12.8	21.4	6.6	10.0	9.1	6.2	0.2	1.6
b. OPEC	14.0	45.2	13.1	-6.8	12.0	0.4	2.7	-1.4
c. All other countries	231.4	375.9	89.3	81.6	124.8	93.8	5.2	58.1
2. Change in U.S. official reserve assets (decrease, +)	14.1	2.4	1.0	1.4	-0.1	0.0	-0.1	-0.2
Private financial flows	505.1	388.3	145.0	138.9	57.0	n.a.	...	...
Banks								
3. Change in net foreign positions of banking offices in the U.S. ¹	15.4	136.1	60.8	29.6	-23.7	6.6	5.2	-45.2
Securities²								
4. Foreign net purchases (+) of U.S. securities	576.8	547.9	121.8	153.7	163.3	221.5	125.0	61.7
a. Treasury securities	133.7	-35.1	-15.9	22.5	45.5	-1.2	16.3	11.8
b. Agency bonds	38.1	21.7	1.7	-10.1	-31.7	17.1	3.8	7.2
c. Corporate and municipal bonds	313.0	412.5	100.1	112.4	105.0	100.4	62.1	15.5
d. Corporate stocks ³	92.0	148.8	35.9	28.8	44.4	105.1	42.7	27.2
5. U.S. net acquisitions (-) of foreign securities	-197.0	-290.4	-52.9	-118.4	-86.7	-87.9	-39.4	-29.5
a. Bonds	-53.1	-152.5	-44.8	-53.8	-42.9	-47.1	-21.9	-14.9
b. Stock purchases	-139.9	-119.1	-8.0	-52.2	-39.6	-40.8	-17.5	-14.6
c. Stock swaps ³	-4.0	-18.8	0.0	-12.4	-4.2	0.0	0.0	0.0
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	7.7	-235.4	-49.0	-66.1	-75.5	n.a.	...	...
7. Foreign direct investment in the U.S.	109.0	180.6	43.0	45.6	23.5	n.a.	...	...
8. Net derivatives (inflow, +)	n.a.	28.8	15.1	-1.2	14.8	n.a.	...	...
9. Foreign acquisitions of U.S. currency	19.0	12.6	1.1	8.4	-1.6	n.a.	...	...
10. Other (inflow, +) ⁴	-25.8	8.0	5.0	87.4	43.0	n.a.	...	...
U.S. current account balance (s.a.)	-754.8	-811.5	-217.3	-187.9	-192.6	n.a.	...	...
Capital account balance (s.a.)⁵	-4.1	-3.9	-0.5	-0.6	-0.6	n.a.	...	...
Statistical discrepancy (s.a.)	-18.5	-17.8	-37.1	-36.6	-9.6	n.a.	...	...

Note. Data in lines 1 through 5 differ in timing and coverage from the balance of payments data published by the Department of Commerce. Details may not sum to totals because of rounding.

1. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements). Includes changes in custody liabilities other than U.S. Treasury bills.

2. Includes commissions on securities transactions and therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. Includes (4d) or represents (5c) stocks acquired through non-market means such as mergers and reincorporations.

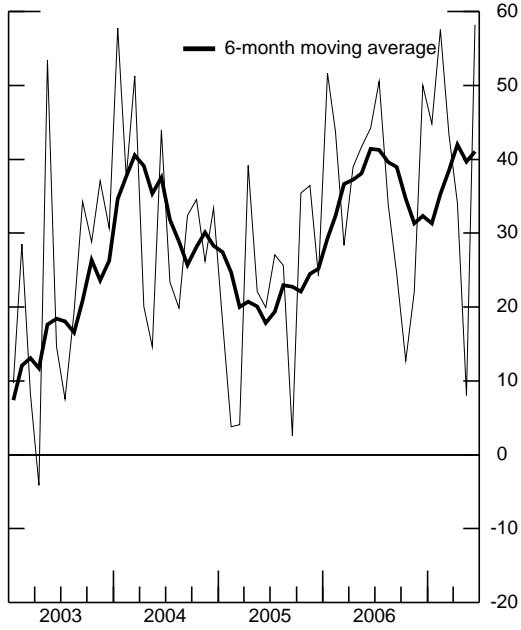
4. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business.

5. Consists of transactions in nonproduced nonfinancial assets and capital transfers.

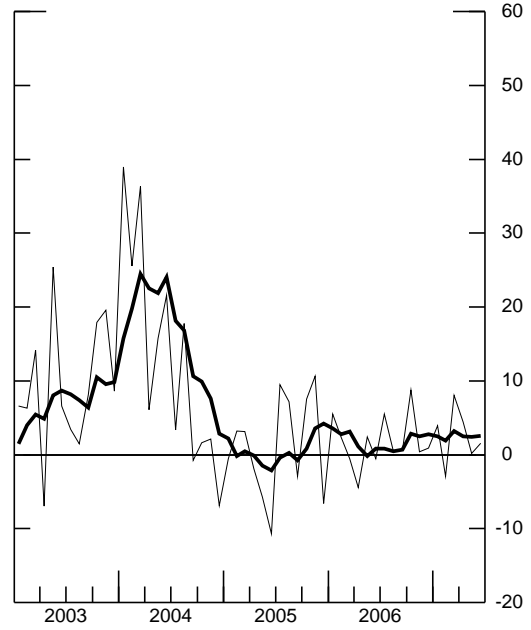
n.a. Not available. ... Not applicable.

Foreign Official Financial Flows Through June 2007 (increase, +)
 (\$ Billions, monthly, not seasonally adjusted)

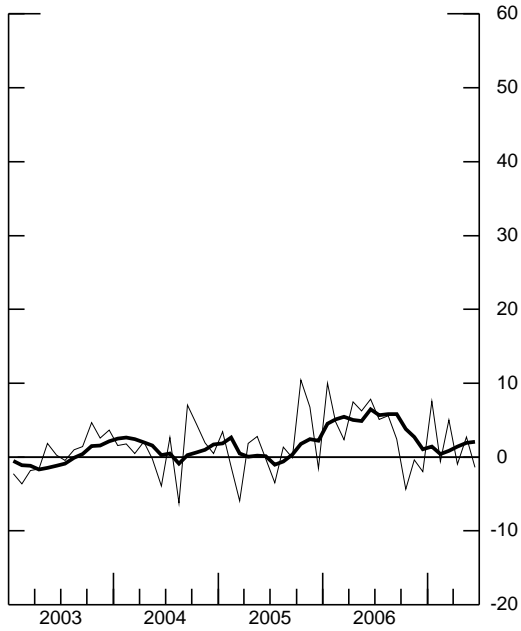
Total



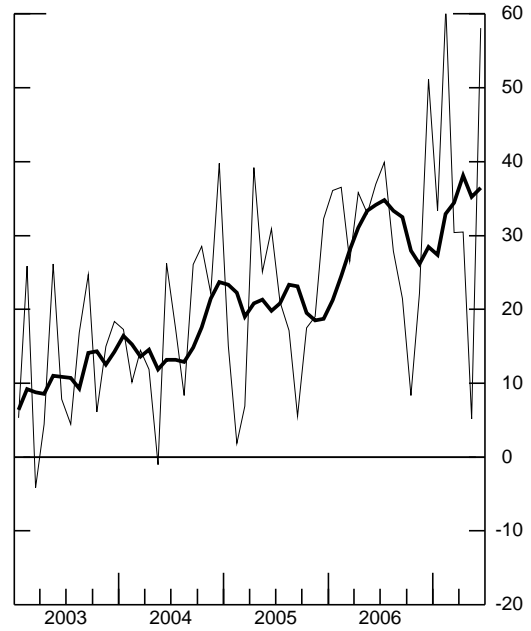
G-10 + ECB



OPEC



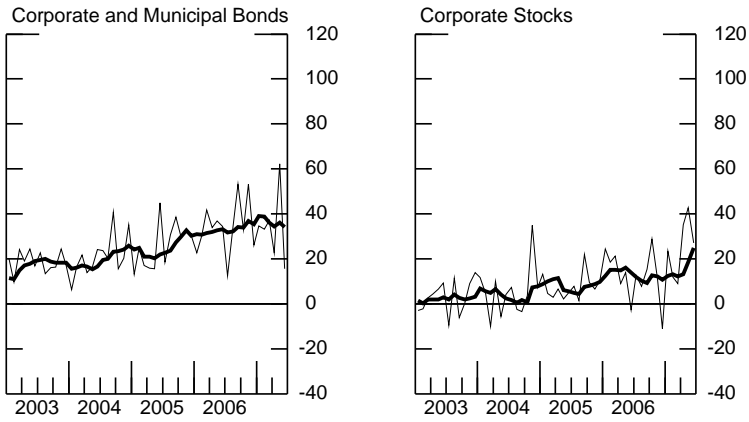
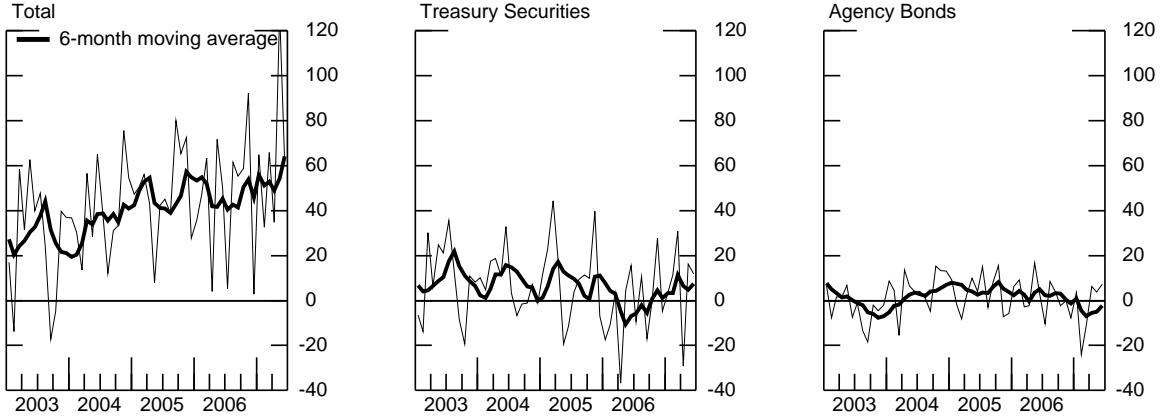
All other countries



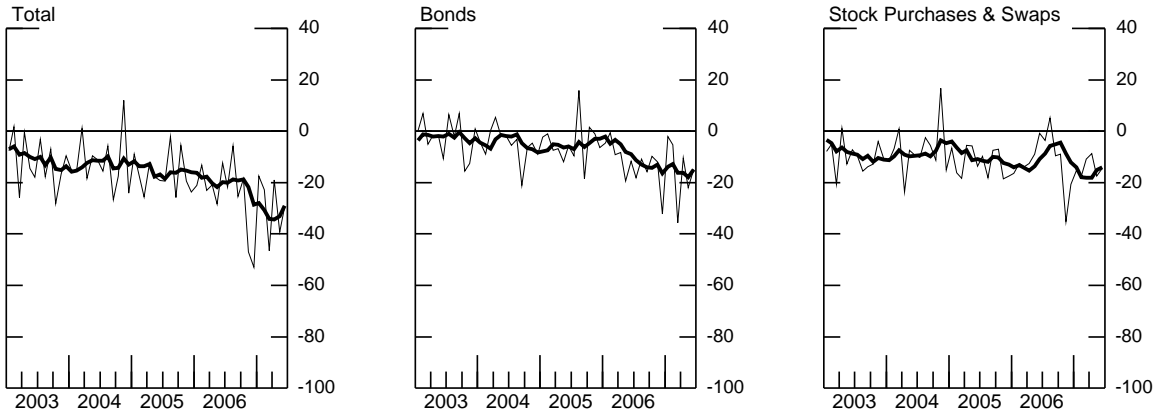
Private Securities Flows Through June 2007

(\$ Billions, monthly, not seasonally adjusted)

Foreign Net Purchases (+) of U.S. Securities



U.S. Net Acquisitions (-) of Foreign Securities



Foreign Financial Markets

Volatility in financial markets increased over the intermeeting period, with sovereign yields falling 10 to 33 basis points and stock markets declining 2.7 to 4.7 percent in major economies. Although these moves were prompted by rising concerns about the subprime-mortgage market in the United States, investors appeared to re-evaluate risk spreads more generally in both U.S. and foreign financial markets and to increase their demands for safer assets. The major currencies index of the dollar's exchange value declined 1.4 percent on balance over the period. On a bilateral basis, the dollar depreciated over 3 percent against the yen, 1.4 percent vis-à-vis the euro and sterling, and it was little changed against the Canadian dollar. In late July, the dollar depreciated against the euro to an all-time low.

Headline equity indexes declined about 4 percent in the United Kingdom and in the euro area, and 4.7 percent in Japan. Following elevated concerns in credit markets, realized volatilities on headline equity indexes picked up in the euro area, Japan, and in the United States over the period.

The intermeeting period saw widespread tightening in monetary policy and increases in short-term interest rates. On June 28, Norway's central bank raised its benchmark rate 25 basis points, to 4.5 percent; on July 5, the Bank of England increased its Bank rate 25 basis points, to 5.75 percent; on July 10, the Bank of Canada raised its target for the overnight rate 25 basis points, to 4.5 percent; and on July 12, the Bank of Japan voted 8-1 to keep its target rate unchanged at 0.5 percent. All moves were fully anticipated. The European Central bank kept its policy rate unchanged at the July and August meetings, also in line with market expectations, and the Bank of England kept the Bank rate unchanged on August 2. Three-month spot interest rates increased 3 to 13 basis points in Germany, the United Kingdom, Japan, and Canada. In contrast, ten-year nominal sovereign yields decreased between 10 and 22 basis points in the same countries. U.S. ten-year rates fell 33 basis points. Yields on inflation-indexed sovereign bonds decreased almost as much as nominal yields did during the intermeeting period, except in the Japan, where inflation breakeven rates rose slightly. Realized volatilities of ten-year bonds increased in the intermeeting period in the United States, Germany, and Japan.

The dollar's trade-weighted exchange value against the currencies of our other important trading partners changed little on balance over the intermeeting period. The dollar depreciated 6.5 percent against the Thai baht, despite Thailand's central bank's

announcement on July 12 that it would scrap limits on direct offshore investment by listed Thai companies in an effort to stem currency appreciation. The Bank of Thailand surprised markets by cutting its benchmark 1-day repurchase rate 25 basis points, to 3.25 percent, on July 18. The dollar also depreciated 2.9 percent vis-à-vis the Brazilian *real*. Brazil's central bank cut its Selic lending rate 50 basis points to a record low of 11.5 percent on July 19. In contrast, the dollar appreciated 1.3 percent vis-à-vis the Mexican peso. The Mexican Bolsa index decreased 2.5 percent on balance, whereas the Brazilian Bovespa index increased 1.1 percent. In emerging Asia, Thailand and Korea's main equity indexes rose over 5 percent on balance. Emerging market bond spreads increased considerably in Latin America over the period.

On July 20, the People's Bank of China (PBoC) increased its benchmark one-year lending and deposit rate floors, effective July 21, following news that both GDP and consumer prices increased strongly in the second quarter. The renminbi appreciated on net 0.7 percent versus the dollar over the intermeeting period and the Shanghai Composite index increased 12.6 percent.

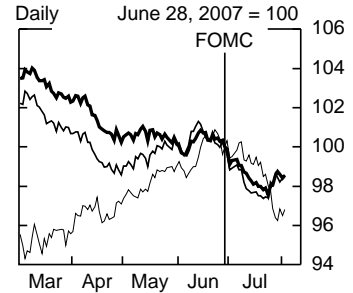
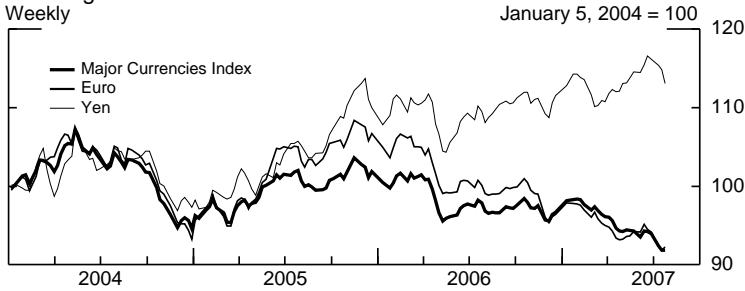
. The Desk did not intervene during the period for the accounts of the System or the Treasury.

Exchange Value of the Dollar and Stock Market Indexes

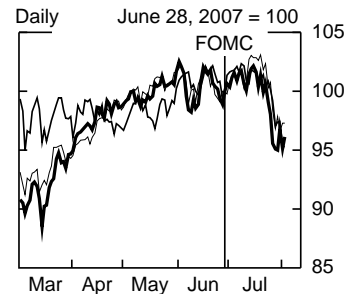
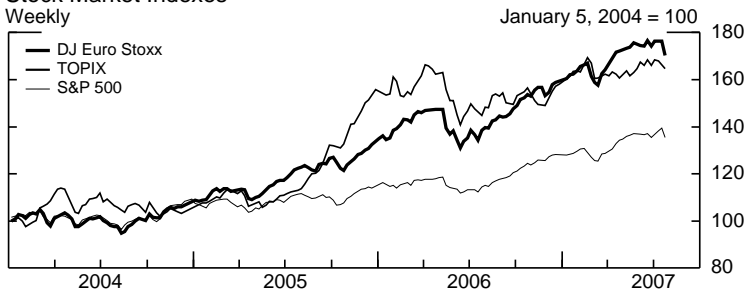
	Latest	Percent change since June FOMC
<i>Exchange rates*</i>		
Euro (\$/euro)	1.3662	-1.4
Yen (¥/\$)	119.1	-3.2
Sterling (\$/£)	2.0300	-1.4
Canadian dollar (C\$/\\$)	1.0577	-0.5
<i>Nominal dollar indexes*</i>		
Broad index	103.0	-0.9
Major currencies index	77.6	-1.4
OITP index	129.7	-0.3
<i>Stock market indexes</i>		
DJ Euro Stoxx	415.1	-3.9
TOPIX	1669.3	-4.7
FTSE 100	6297.8	-4.2
S&P 500	1466.0	-2.7

* Positive percent change denotes appreciation of U.S. dollar.

Exchange Value of the Dollar
Weekly



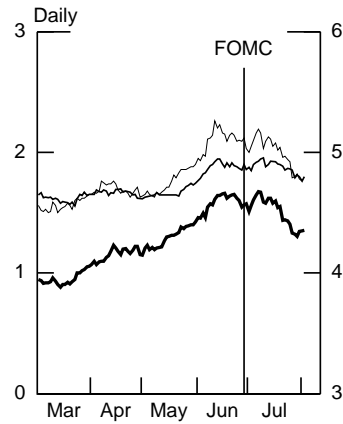
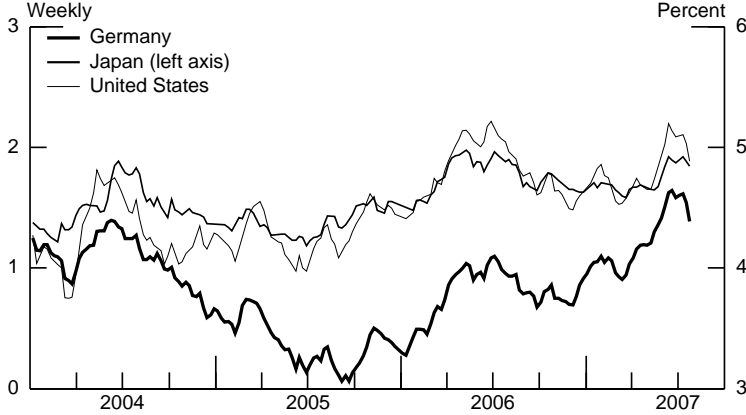
Stock Market Indexes
Weekly



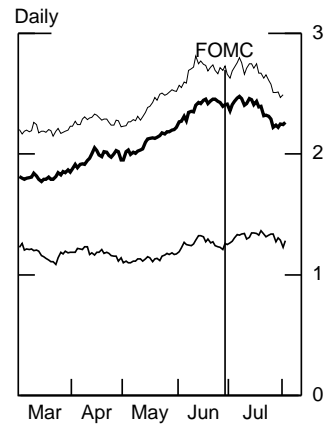
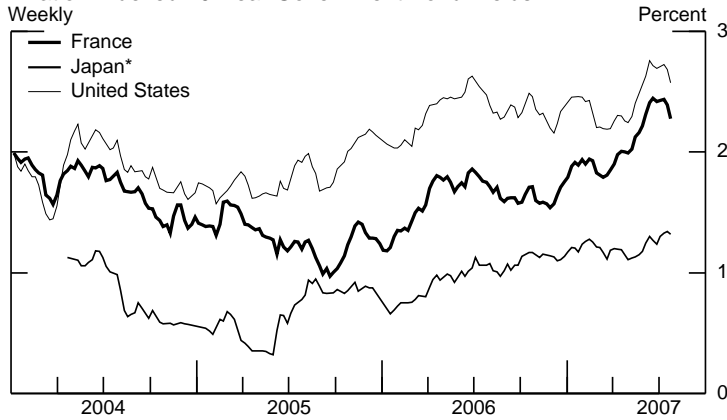
Industrial Countries: Nominal and Real Interest Rates

	3-month LIBOR		10-year nominal		10-year indexed		Percent
	Latest	Change since June FOMC	Latest	Change since June FOMC	Latest	Change since June FOMC	
Germany	4.28	0.11	4.36	-0.21	2.28	-0.19	
Japan	0.79	0.03	1.80	-0.10	1.28	0.02	
United Kingdom	6.06	0.09	5.22	-0.22	2.06	-0.15	
Canada	4.68	0.13	4.51	-0.12	...	...
United States	5.36	0.00	4.76	-0.33	2.49	-0.20	

Nominal 10-Year Government Bond Yields



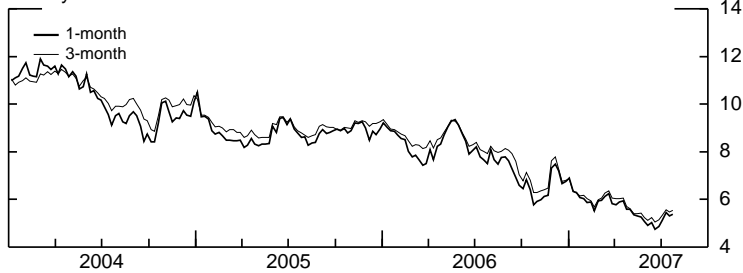
Inflation-Indexed 10-Year Government Bond Yields



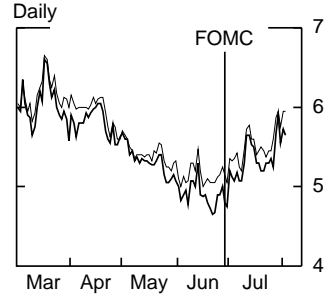
*Japan first issued inflation-indexed debt in March 2004.

Measures of Market Volatility

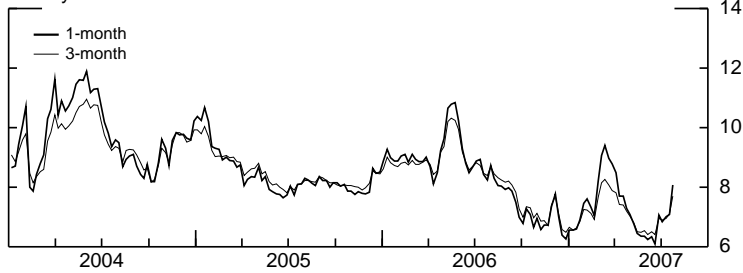
Dollar-Euro Options-Implied Volatility*
Weekly



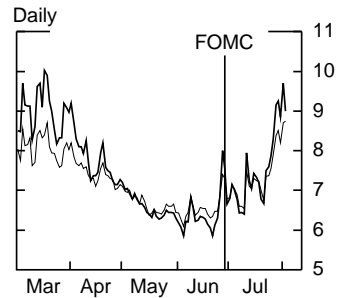
*Derived from at-the-money options.



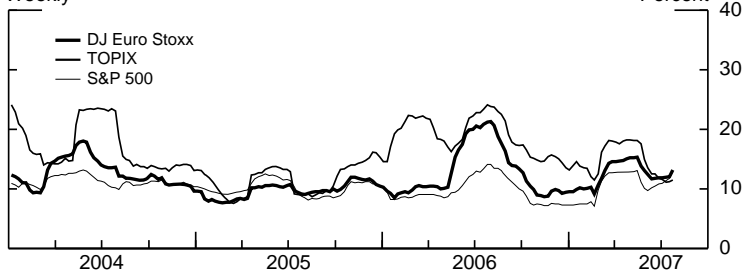
Yen-Dollar Options-Implied Volatility*
Weekly



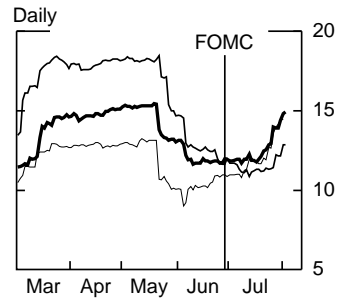
*Derived from at-the-money options.



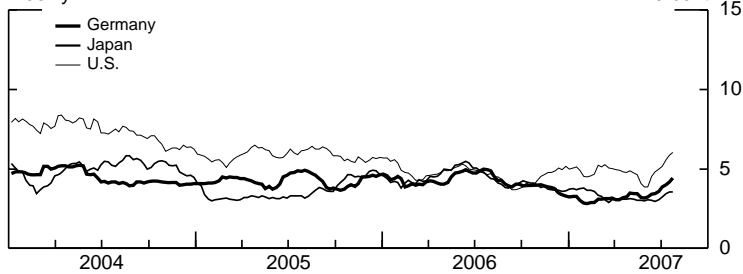
Realized Stock Market Volatility*
Weekly



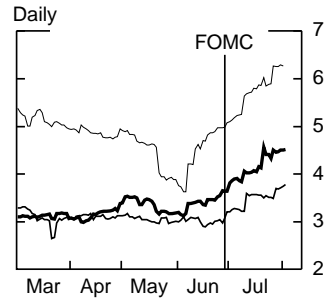
*Annualized standard deviation of 60-day window of daily returns.



Realized 10-Year Bond Volatility*
Weekly



*Annualized standard deviation of 60-day window of daily returns.

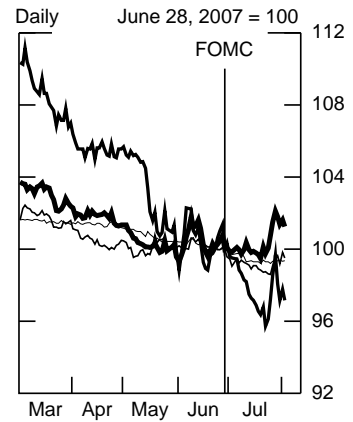
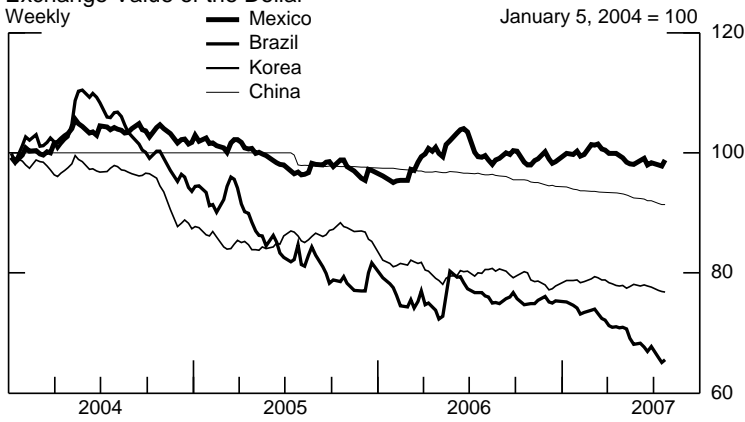


Emerging Markets: Exchange Rates and Stock Market Indexes

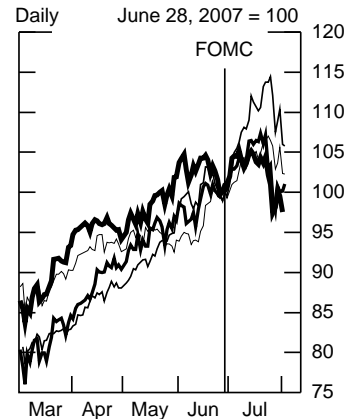
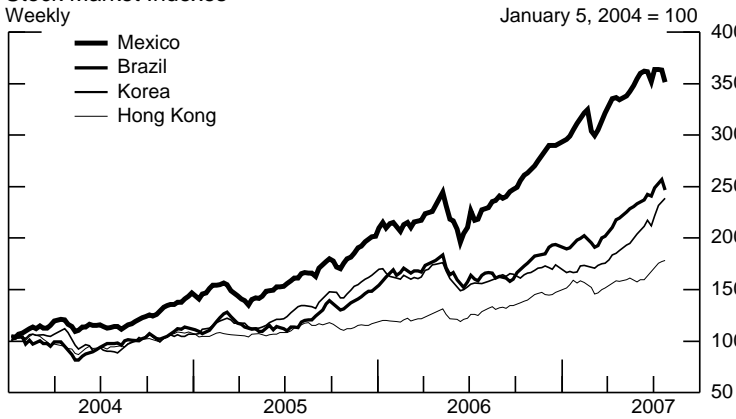
	Exchange value of the dollar		Stock market index	
	Latest	Percent change since June FOMC*	Latest	Percent change since June FOMC
Mexico	10.9205	1.3	30048	-2.5
Brazil	1.8690	-2.9	54725	1.1
Venezuela	2144.60	0.0	42230	7.1
China	7.5713	-0.6	4408	12.6
Hong Kong	7.8287	0.2	22443	2.3
Korea	922.1	-0.5	1853	5.8
Taiwan	32.88	0.2	8951	0.6
Singapore	1.5173	-1.0	948	-3.5
Thailand	29.60	-6.5	830	6.8

* Positive percent change denotes appreciation of U.S. dollar.

Exchange Value of the Dollar
Weekly



Stock Market Indexes
Weekly



Emerging Markets: Short-Term Interest Rates and Dollar-Denominated Bond Spreads

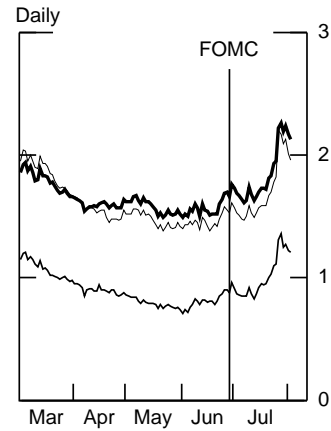
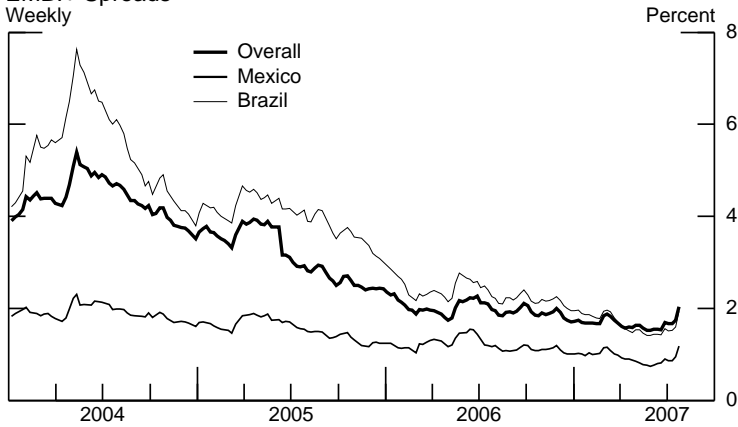
	Short-term interest rates*		Dollar-denominated bond spreads**	
	Latest	Change since June FOMC	Latest	Change since June FOMC
Mexico	7.25	0.00	1.21	0.31
Brazil	11.62	-0.35	1.96	0.41
Argentina	11.50	2.38	4.33	1.08
China	...	...	0.64	0.09
Korea	4.90	0.15	...	...
Taiwan	2.62	0.10	...	...
Singapore	3.50	0.00	...	...
Hong Kong	4.18	-0.28	...	...

*One month interest rate except 1-week rate for Korea. No reliable short-term interest rate exists for China.

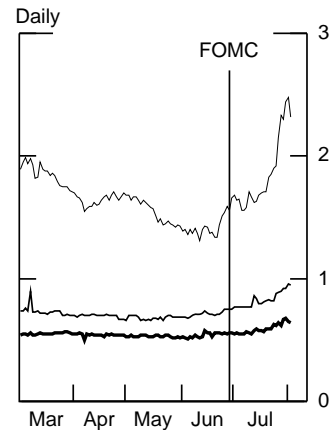
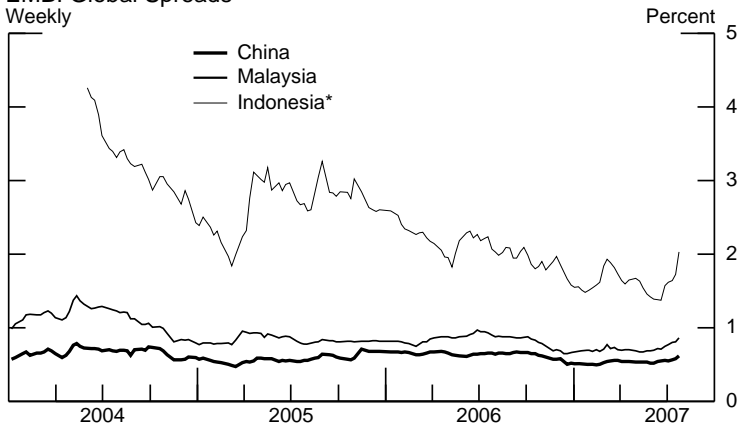
**EMBI+ or EMBI Global Spreads over similar-maturity U.S. Treasuries.

... Korea, Taiwan, Singapore, and Hong Kong have no outstanding dollar-denominated sovereign bonds.

EMBI+ Spreads
Weekly



EMBI Global Spreads
Weekly



*Begins May 2004.

Developments in Advanced Foreign Economies

Upbeat business and consumer confidence, as well as favorable labor market conditions, suggests that growth has remained above trend in all the advanced foreign economies in the current quarter, despite some slowing of expansion in the second quarter. Although many of these economies experienced sharp declines in equity prices and widening credit spreads amid deepening concerns about credit quality, these developments occurred too late in the intermeeting period to have any apparent impact on incoming data.

Headline inflation has leveled off in both the United Kingdom and Canada, but elevated core inflation readings reveal that inflationary pressures are still strong. In the euro area, inflation continues to hover close to, but below, 2 percent. In Japan, headline inflation dipped back into negative territory in June. The Bank of England and the Bank of Canada both raised their policy interest rates in early July.

In Japan, the June Tankan survey continued to portray an economy that is expanding moderately, with the headline index of economic sentiment among large manufacturers remaining high by historical standards. The survey also pointed to strong capital spending plans by large- and medium-sized firms and indicated an across-the-board improvement in the sales outlook. Overall, firms continued to see the labor market and resource utilization as relatively tight.

Nevertheless, recent indicators suggest that the economy is facing some headwinds. Second-quarter consumption indicators are somewhat mixed, with retail sales advancing in May and real household expenditures receding a bit in both May and June. Industrial production rebounded 1.2 percent in June after declining for three consecutive months. Shipments continued to rise in June, leading to a reduction in the inventories-to-sales ratio. The inventories-to-sales ratio for information and communications equipment also fell in May and June, after having risen substantially in previous months. In June, real exports rose 0.7 percent, while real imports were about unchanged. On a twelve-month basis, real exports to the United States declined for a fourth consecutive month in June, while real exports to the European Union and Asia continued to increase.

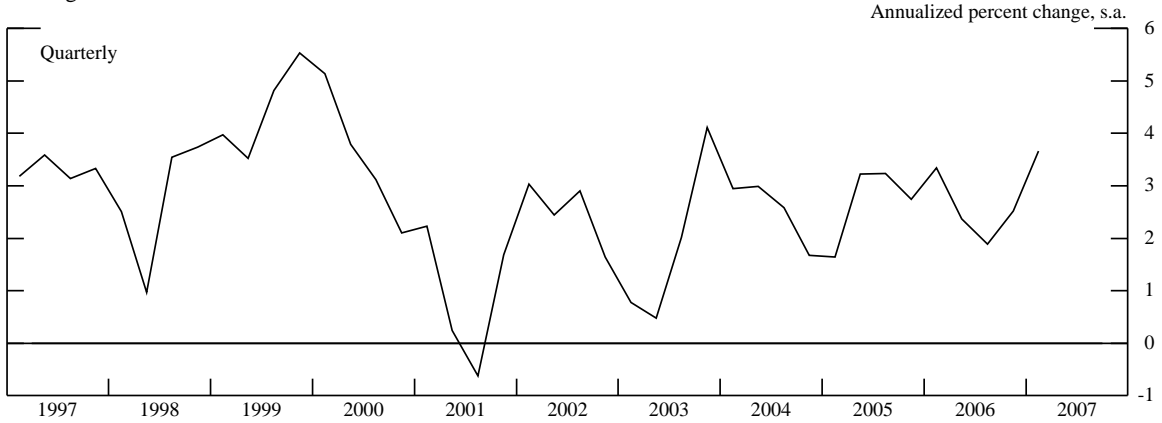
Consumer prices edged lower in June, and the twelve-month rate of headline inflation turned negative again. The twelve-month rate of core inflation remained slightly below zero in June, and the fall in Tokyo core consumer prices in July indicated little inflationary pressure in the near term. Nominal wages continued to decline in May,

despite the unemployment rate remaining at 3.7 percent, the lowest rate in nearly ten years.

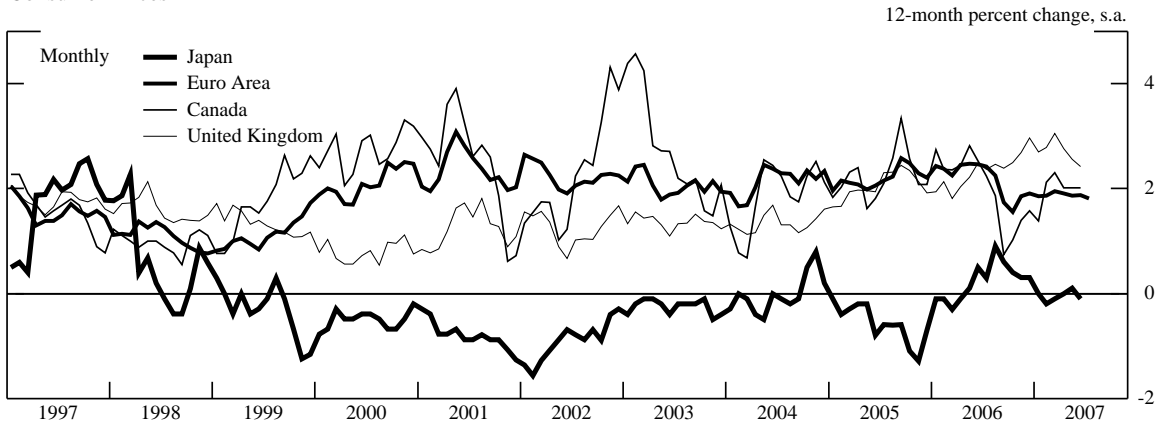
In Upper House elections held July 29, Japan's ruling Liberal Democratic Party lost its majority. Prime Minister Abe vowed to continue pursuing reform despite calls for his resignation, but he said he would reshuffle his cabinet in an effort to win back voter trust. The ruling coalition still has a large majority in the more powerful Lower House of Parliament, but loss of control of the upper chamber may threaten policy gridlock.

Advanced Foreign Economies

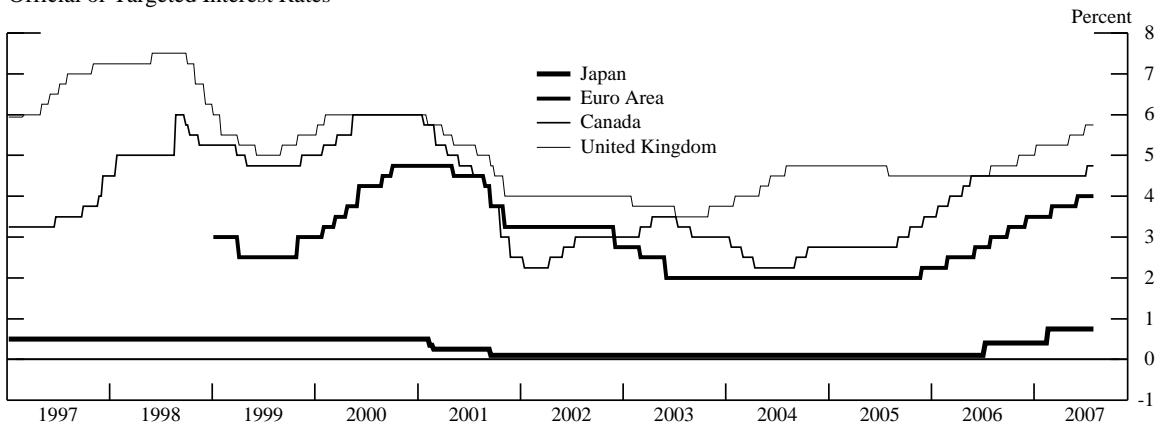
Average Real GDP*



Consumer Prices

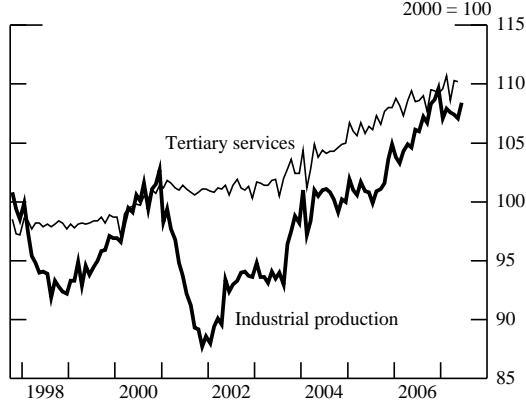


Official or Targeted Interest Rates

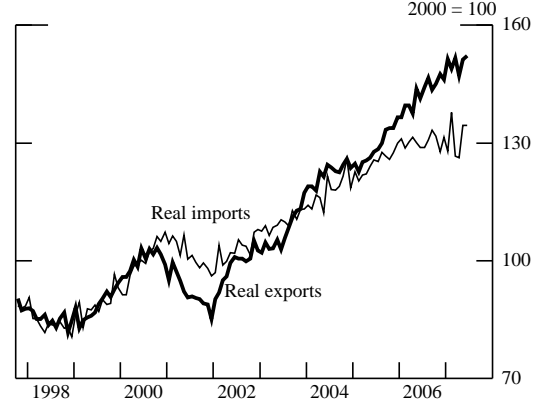


Japan

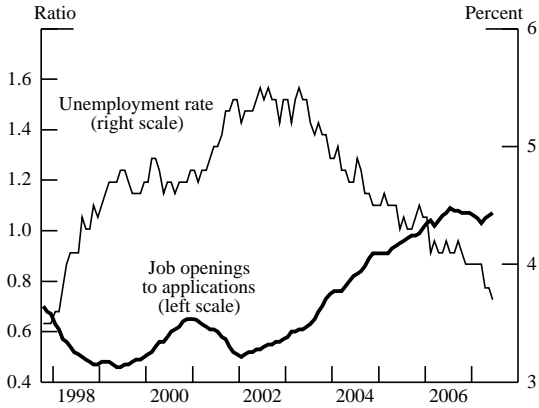
Economic Activity



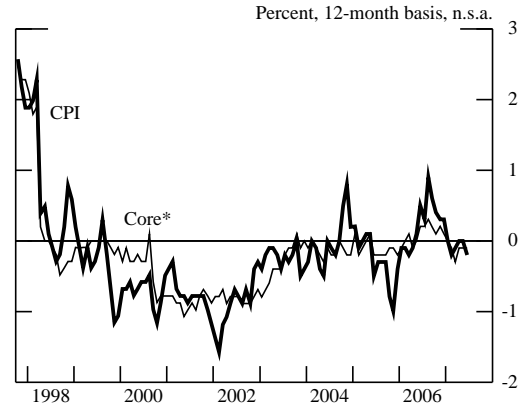
Real Trade



Labor Market



Consumer Price Inflation



Economic Indicators

(Percent change from previous period except as noted, s.a.)

Indicator	2006		2007		2007		
	Q4	Q1	Q2	Apr.	May	June	July
Housing starts	3.4	-4.6	1.2	-1.0	-10.6	17.3	n.a.
Machinery orders ¹	0.3	-0.7	n.a.	2.2	5.9	n.a.	n.a.
Household expenditures	1.6	1.0	-0.1	0.6	-0.2	-0.2	n.a.
New car registrations	-2.1	-1.3	-2.5	0.2	0.3	-1.9	-2.9
Business sentiment ²	8.0	8.0	7.0	...	...	...	...
Wholesale prices ³	2.6	1.9	2.3	2.3	2.2	2.3	n.a.

1. Private sector, excluding ships and electric power.

2. Tankan survey, diffusion index. Level.

3. Percent change from year earlier, n.s.a.

n.a. Not available. ... Not applicable.

Euro-area GDP growth in the first quarter was revised upward 0.5 percentage point to 2.9 percent. The pace of economic expansion appears to have slowed a bit in the second quarter in spite of a rebound in consumption spending in Germany from the first-quarter plunge that was induced by a hike in the value-added tax. Other data released during the intermeeting period came in a bit weaker than had been expected. Euro-area industrial production rose in May, but the average figure for April and May was just 0.2 percent above the first-quarter average. Euro-area retail sales also disappointed, with a decline of 0.7 percent in May, reportedly because of unusually gloomy weather conditions. In June, in contrast, French consumer spending on manufactured goods bounced back after two weak months, rising 1.6 percent.

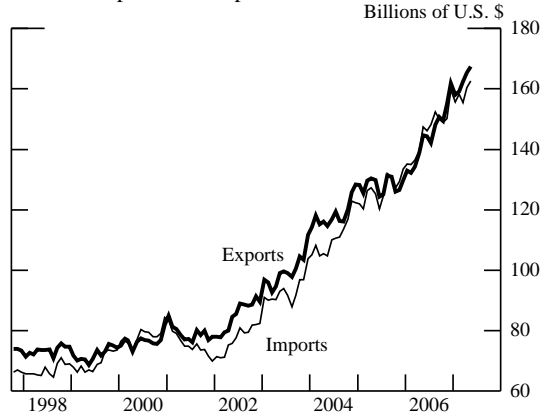
Indicators of third-quarter activity point to relatively strong growth. The euro-area purchasing managers' index for manufacturing and especially for services remained well above the expansion threshold in July. European Commission survey measures of business and consumer confidence remained near record levels in July. In Germany, the IFO indicator of business morale edged down for a second straight month in July but remained at a fairly elevated level, even though manufacturers were less optimistic about exports.

Labor market conditions have continued to improve. The euro-area unemployment rate declined further in May to 6.9 percent, and remained there in June, the lowest rate since Eurostat began measuring it in 1993 and almost 2 percentage points below its rate at the beginning of 2005. Wage pressures have nonetheless remained moderate. In the first quarter, total labor costs and unit labor costs rose only 2.2 percent and 0.8 percent, respectively, above their levels a year earlier.

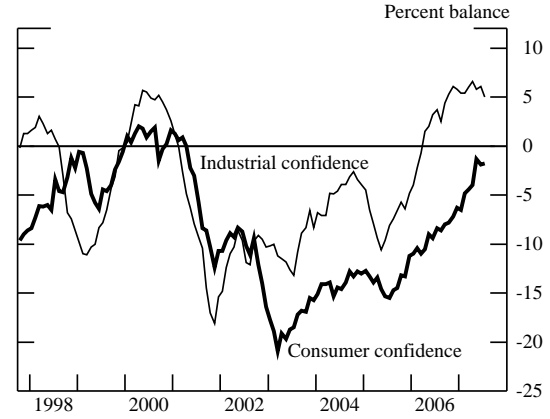
Euro-area consumer prices rose 1.8 percent in July on a twelve-month basis, according to the preliminary estimate. Core inflation (excluding energy and unprocessed food) stood at 1.9 percent in June. Liquidity growth in the euro area has remained surprisingly high, renewing concern about price stability among several ECB officials.

Euro Area

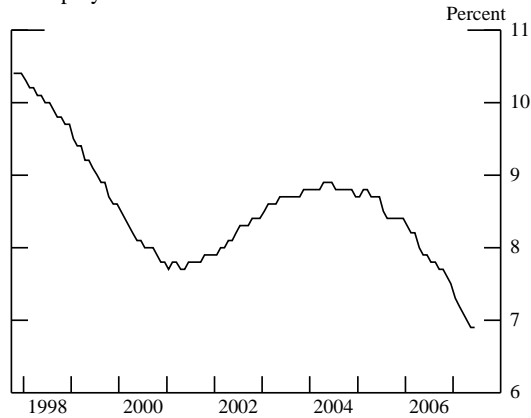
Nominal Exports and Imports



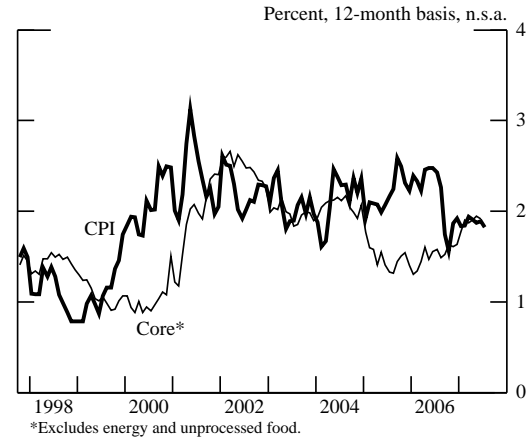
Economic Sentiment



Unemployment Rate



Consumer Price Inflation



Economic Indicators
(Percent change from previous period except as noted, s.a.)

Indicator	2006	2007		2007			
	Q4	Q1	Q2	Mar.	Apr.	May	June
Industrial production ¹	0.6	0.9	n.a.	0.6	-0.9	0.9	n.a.
Retail sales volume ²	0.3	0.0	n.a.	0.6	-0.1	-0.7	n.a.
New car registrations	3.5	-2.1	0.3	4.4	-5.4	4.3	1.4
Employment	0.3	0.4	n.a.	...	...	...	...
Producer prices ³	4.1	3.0	2.4	2.8	2.5	2.4	2.3
M3 ³	9.9	11.0	10.9	11.0	10.3	10.6	10.9

1. Excludes construction.
 2. Excludes motor vehicles.
 3. Eurostat harmonized definition. Percent change from year earlier, s.a.
 n.a. Not available. ... Not applicable.

Real GDP in the **United Kingdom** rose 3.3 percent (a.r.) in the second quarter, according to the preliminary estimate. Growth was driven mainly by services, which expanded 3.6 percent. After four quarters of stagnation, the output of production industries expanded 2.0 percent, led by a 2.7 percent expansion of manufacturing.

Although GDP expenditure components are not yet available, other indicators are consistent with a firming of domestic demand in the second quarter. Retail sales grew a robust 4.7 percent (a.r.) in the three-month period to June, up 2.6 percentage points from a quarter earlier. According to the Bank of England Agents' Summary of Business Conditions, a survey of U.K. private businesses, investment intentions in the services and manufacturing sectors were both near decade highs in June.

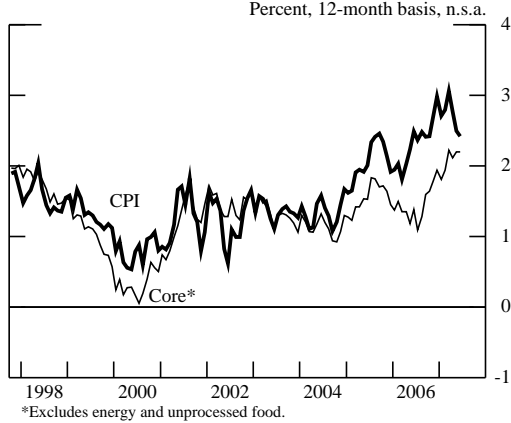
The Labor Force Survey and the claimant count measures of the unemployment rate both ticked down during the intermeeting period, reaching 5.4 percent in April and 2.7 percent in June, respectively. Wage inflation remains contained. The twelve-month growth rate of average earnings (including bonuses) was 3.5 percent in May, almost 0.5 percentage points lower than its average over the previous five years. Unit wage costs in manufacturing industries were 1.3 percent higher in May than they were a year earlier.

The twelve-month rate of headline inflation continued to revert back towards the 2 percent target during the intermeeting period, sliding to 2.4 percent in June. For a fourth consecutive month, housing and household services were the main drivers of the fall in inflation, as natural gas and electricity prices declined so far this year after having risen last year. Core inflation, which excludes energy and unprocessed food, was unchanged at 2.2 percent in June, remaining near record highs since the series began in 1997.

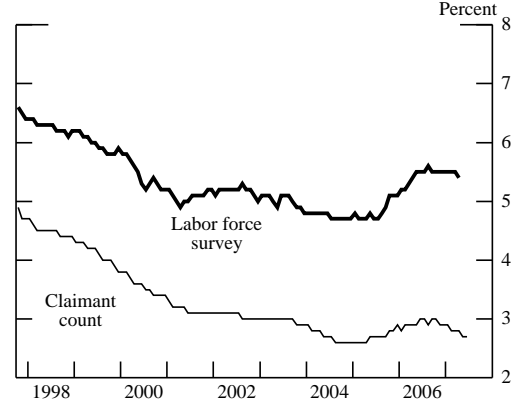
The Bank of England raised its key policy interest rate $\frac{1}{4}$ percentage point to 5.75 percent on July 5, judging that the balance of risks to the outlook for inflation continued to lie to the upside.

United Kingdom

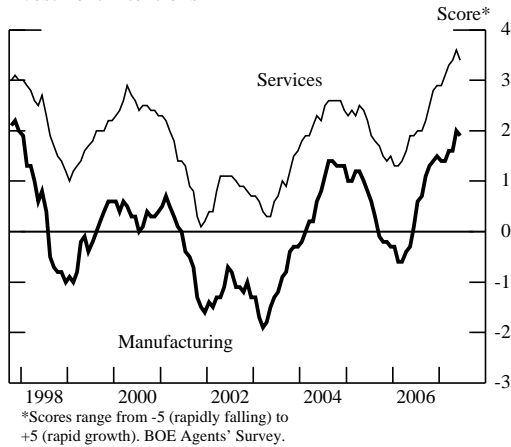
Consumer Price Inflation



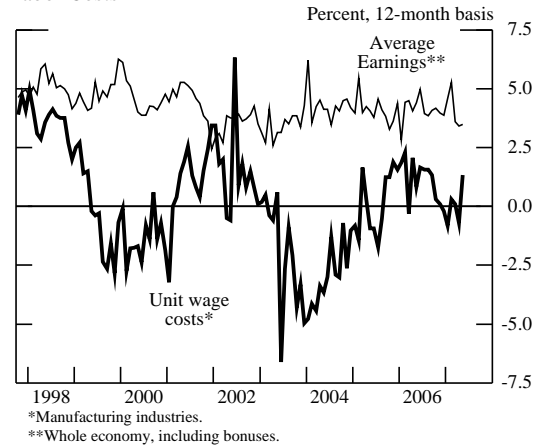
Unemployment Rates



Investment Intentions



Labor Costs



Economic Indicators

(Percent change from previous period except as noted, s.a.)

Indicator	2006	2007		2007			
	Q4	Q1	Q2	Apr.	May	June	July
Real GDP	3.3	2.8	3.3	...	...	...	...
PMI Services ¹	59.9	58.1	57.4	57.3	57.2	57.7	n.a.
Industrial production	-0.2	-0.1	n.a.	0.3	0.6	n.a.	n.a.
Business confidence ²	8.3	20.3	20.3	18.0	18.0	25.0	10.0
Consumer confidence ²	-4.9	-6.2	-4.2	-6.6	-3.2	-2.9	-2.8
Trade balance ³	-23.3	-24.1	n.a.	-8.3	-7.0	n.a.	n.a.

1. 50+ indicates expansion.

2. Percent balance. 3. Level in billions of US Dollars.

n.a. Not available. ... Not applicable.

In **Canada**, real GDP by industry rose 4.2 percent (a.r.) in May, propelled by significant increases in retail and wholesale trade. The advance in retail trade between April and May, which was widespread across sectors, was the best one-month showing since late 2001. Construction activity also increased, as strong growth in non-residential construction more than offset a small decline in residential construction. Manufacturing output rose; however, industrial production slipped a bit, due to a retreat of energy sector output, especially in oil and gas exploration activities.

Other indicators for the second quarter continue to suggest growth at a rate slightly above that of potential. Averaged over April and May, the volume of exports was over one percent higher than the first-quarter average, while the volume of imports was about 0.6 percent higher. Despite appreciation of the Canadian dollar, the manufacturing sector, which is heavily export-oriented, has fared particularly well: the volume of manufacturing shipments increased for a fourth consecutive month in May, and both new and unfilled orders also rose strongly. Second-quarter housing starts were 2 percent above their first-quarter level. The composite index of leading indicators and the Ivey purchasing managers' index both rose again in June.

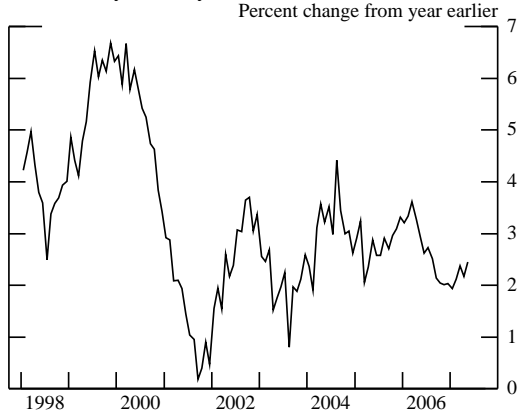
Employment growth picked up in June after being about flat on net in the previous two months; the April and May lull came on the heels of first-quarter job gains that were the strongest in five years. The unemployment rate again held steady at 6.1 percent in June, a thirty-three year low, and twelve-month wage inflation increased to 3.2 percent from 2.8 percent in May.

In June, the twelve-month rate of consumer price inflation was 2.2 percent, the fifth consecutive month it has been above the mid-point of the Bank of Canada's target range of 1 to 3 percent. The twelve-month rate of core inflation, which excludes the eight most volatile components and the effects of changes in indirect taxes, moved up to 2.5 percent in June from 2.2 percent in May. Continuing to exert upward pressure on the core index is homeowners' replacement costs (which are estimated using, among other data, prices for new homes); replacement costs have decelerated since last summer, but they continue to grow at over 6 percent. The twelve-month rate of change of new home prices inched down to 8.6 percent in May, continuing its gradual moderation since last summer.

The Bank of Canada increased the target for the overnight rate $\frac{1}{4}$ percentage point to 4.5 percent on July 10, its first move since May 2006, citing stronger-than-expected economic growth and inflation in the first half of this year.

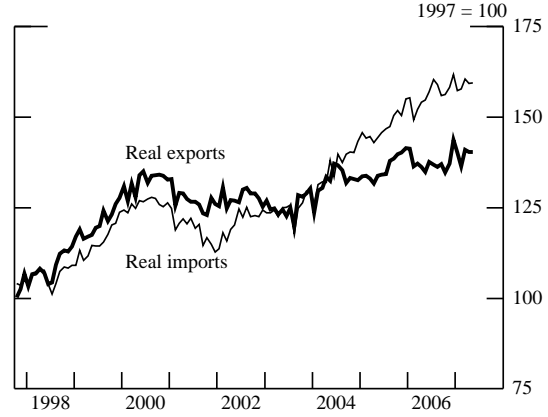
Canada

Real GDP by Industry*

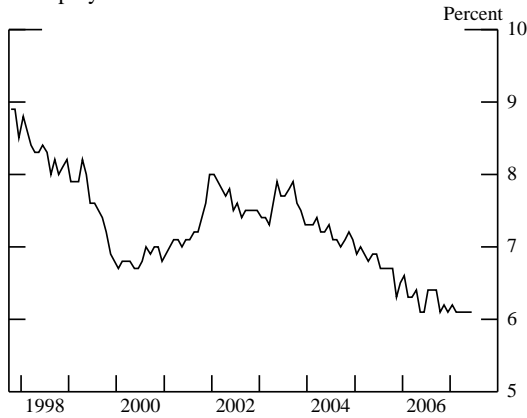


*Constructed from various Statistics Canada surveys and supplements the quarterly income and expenditure-based estimates.

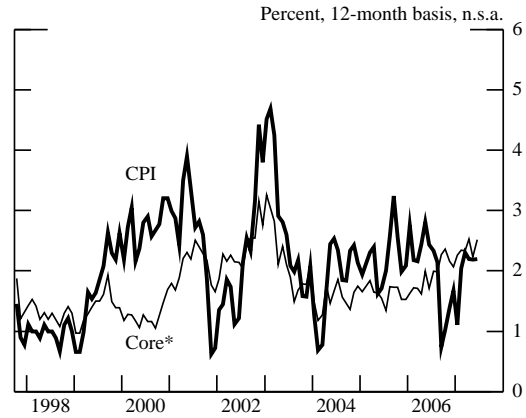
Real Trade



Unemployment Rate



Consumer Price Inflation



*Excludes 8 most volatile components and the effects of changes in indirect taxes.

Economic Indicators
(Percent change from previous period except as noted, s.a.)

Indicator	2006	2007		2007			
	Q4	Q1	Q2	Mar.	Apr.	May	June
Industrial production	-1.1	0.8	n.a.	0.1	-0.0	-0.2	n.a.
New manufacturing orders	1.5	0.8	n.a.	-1.2	-0.7	2.1	n.a.
Retail sales	0.7	1.0	n.a.	1.4	0.3	2.5	n.a.
Employment	0.6	1.0	0.3	0.3	-0.0	0.1	0.2
Consumer attitudes ¹	99.7	98.3	n.a.	...	...	...	...
Business confidence ¹	148.1	139.9	n.a.	...	...	...	...

1. 1991=100.
n.a. Not available. ... Not applicable.

Economic Situation in Other Countries

Recent economic indicators from the developing economies suggest that economic activity remains generally strong. The Chinese economy has continued to expand at a blistering pace, and activity elsewhere in emerging Asia appears to have accelerated. In Latin America, Mexican indicators point to a weaker-than-expected rebound in the second quarter, whereas Brazil and Argentina appear to have experienced solid growth. Inflation has increased in China, mainly due to soaring food prices, but has generally remained little changed elsewhere in the developing world. Equity prices have fallen and bond spreads have widened in several emerging market economies, particularly in Latin America; however, there is no evidence so far that this increased volatility has weighed on economic activity.

In **China**, second-quarter real GDP grew at an estimated 14¾ percent annual rate, driven by strength of exports and fixed investment. The rise in output from its year-earlier level was the fastest recorded rate in nearly twelve years. Exports have been spurred by both high global demand and a rush to ship goods before the imposition of a fresh round of cuts in value-added tax rebates, effective July 1, on a wide array of exported products. Ballooning exports have resulted in another large increase in the trade surplus. Fixed investment continued to expand rapidly, up 28 percent in the second quarter from its year-earlier level, and retail sales grew at an impressive pace of more than 15 percent.

Consumer prices accelerated further in June, with a twelve-month increase of 4¼ percent, up from 3½ percent in May. Food prices continued to soar, rising more than 11 percent in the twelve months ending in June. Non-food price inflation hovered at just 1 percent, but concerns about food price inflation spilling into non-food price inflation have intensified. Part of the acceleration in food prices is due to rising meat prices resulting from hog disease earlier this year. Moreover, the rate of inflation of grain prices has not fallen. Chinese authorities tightened monetary policy again in mid-July after the release of the second quarter's much-higher-than-expected growth and inflation figures. Interest rates on the benchmark one-year deposit and lending rates were increased by 27 basis points each, to 3.33 and 6.84 percent respectively, the third increase in rates this year. In late July, the reserve requirement ratio for banks was raised by ½ percentage point, effective August 15. Reserve requirements have been raised a cumulative 4.5 percentage points since June 2006, bringing the total ratio to 12 percent for large banks.

Chinese Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	10.0	10.4	14.2	14.7	...	...	...
Industrial production	17.2	14.3	4.1	8.1	-1	.1	6.0
Consumer prices ²	1.5	2.7	2.8	3.6	3.0	3.5	4.2
Merch. trade balance ³	102.0	177.5	249.5	280.7	236.8	295.3	310.0

1. Annual rate. Quarterly data estimated by staff from reported four-quarter growth rates. Annual data are Q4/Q4.

2. Percent change from year-earlier period, except annual data, which are Dec./Dec.

3. Billions of U.S. dollars, annual rate. Imports are c.i.f.

... Not applicable.

In **Hong Kong**, recent data point to a pickup in the pace of real GDP growth in the second quarter, following below-trend growth in the first. Retail sales rebounded in May from a weak April level. In addition, the value of exports and imports in the second quarter grew 11 and 12 percent from a year earlier, respectively, an indicator of strong activity in this entrepôt economy. The unemployment rate fell to its lowest level since 1998. Twelve-month inflation remained low in May and June because of a rent concession on public housing, scheduled to expire in October.

Hong Kong Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	7.8	7.2	2.0	n.a.	...	...	...
Unemployment rate ²	5.7	4.8	4.3	4.2	4.3	4.3	4.2
Consumer prices ³	1.4	2.3	1.7	1.3	1.4	1.3	1.4
Merch. trade balance ⁴	-10.5	-17.9	-17.6	-18.8	-12.0	-9.4	-35.1

1. Annual rate. Annual data are Q4/Q4.

2. Percent. Monthly data are averages of the current and previous two months.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

n.a. Not available. ... Not applicable.

In **Taiwan**, economic indicators suggest that output growth increased in the second quarter from a first-quarter trough. After contracting in the first quarter, industrial production jumped nearly 8 percent in the second. In addition, trade data for June showed strong growth in both exports and imports, with the merchandise trade surplus

increasing. In June, twelve-month consumer price inflation remained near zero; however, consumer prices climbed in the first half of this year following a fall in the second half of 2006. The central bank in June increased its official discount rate to 3.125 percent, the highest level since September 2001, mainly to discourage the carry trade that has targeted Taiwan because of its low interest rates.

Taiwan Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	6.5	4.0	1.6	n.a.	...	...	...
Unemployment rate ²	4.1	3.9	3.9	3.9	4.0	4.0	3.9
Industrial production	4.6	5.0	-1.0	7.9	2.6	3.8	1.7
Consumer prices ³	2.2	.7	1.0	.2	.7	.0	.1
Merch. trade balance ⁴	7.8	11.6	15.2	11.5	6.4	11.6	16.6
Current account ⁵	16.0	24.7	35.1	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

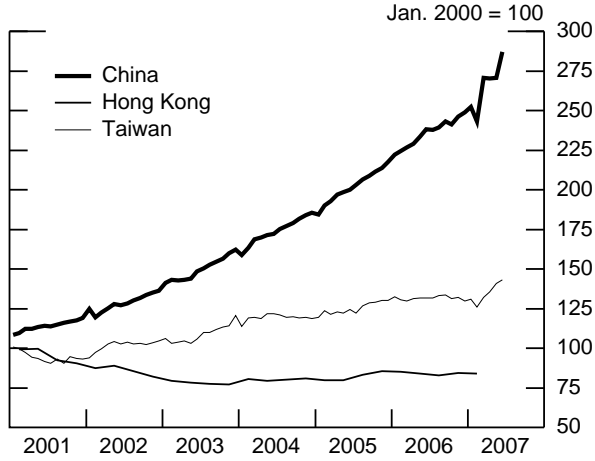
4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

5. Billions of U.S. dollars, n.s.a., annual rate.

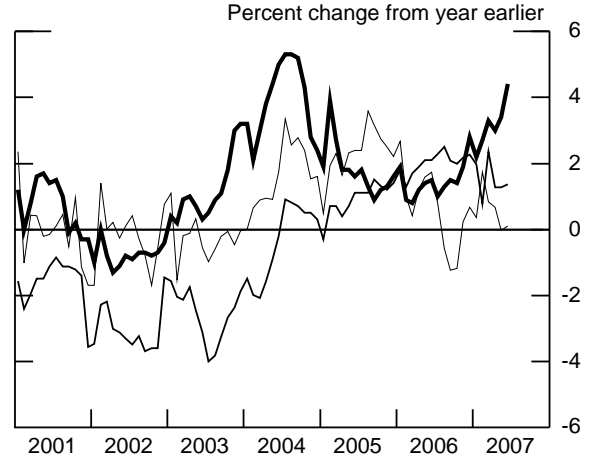
n.a. Not available. ... Not applicable.

China, Hong Kong, and Taiwan

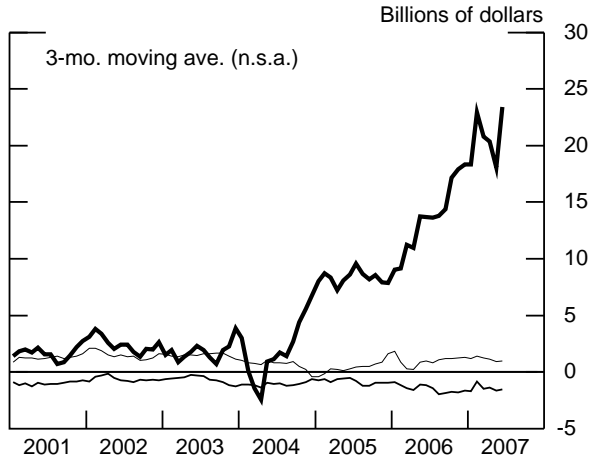
Industrial Production



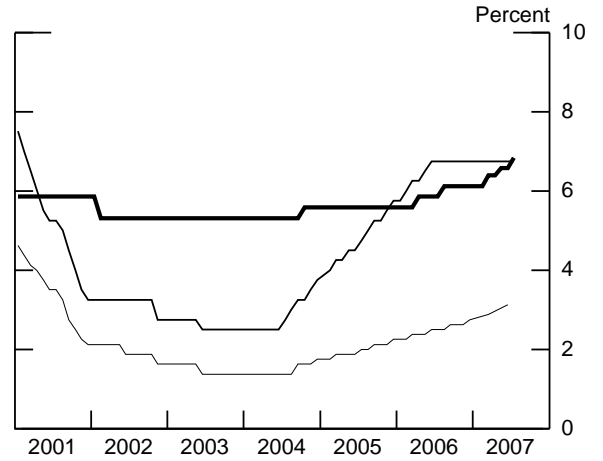
Consumer Prices



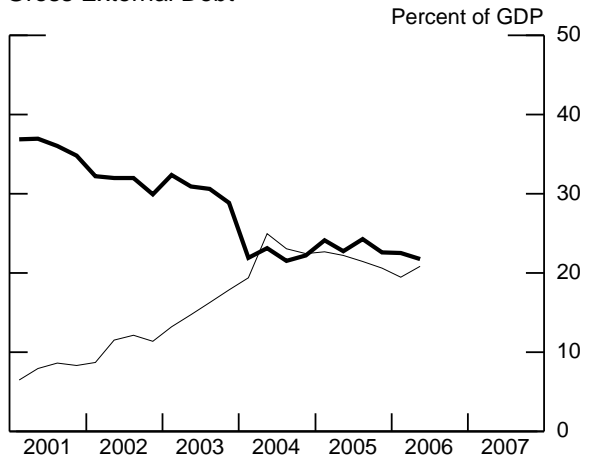
Merchandise Trade Balances



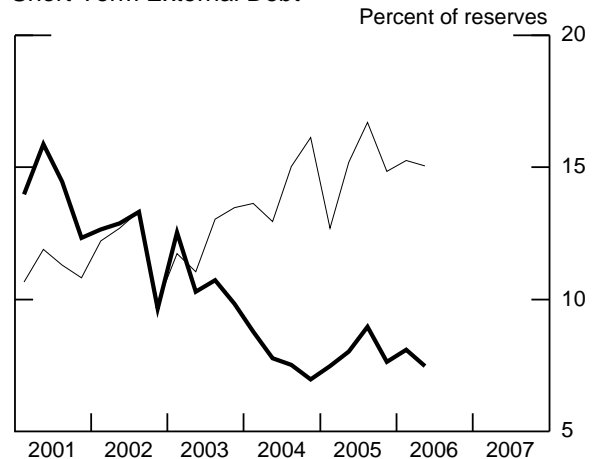
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



Korean GDP jumped 7 percent in the second quarter, a notable acceleration from the previous two quarters. Domestic demand remained strong, and net exports rebounded some. On the back of the solid trade performance, Korea's current account returned to surplus in the second quarter. Twelve-month consumer price inflation in Korea rose 2.5 percent in July. Korean inflation continues to be boosted by food prices and a shift up in core inflation from last year. Bank credit has risen sharply with lending to small- and medium-sized establishments up over 20 percent in the twelve months ending in June. In response, the Bank of Korea raised its target rate $\frac{1}{4}$ percentage point to 4.75 percent in mid-July and also announced restrictions on overseas borrowing by foreign and domestic banks. Short-term external debt has soared of late, in part reflecting currency hedging by Korean shipbuilders. Finally, the Bank also stated that it would be shifting its target rate from the call rate to a 7-day repo rate early next year, but provided few details.

Korean Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	May	Jun.	Jul.
Real GDP ¹	5.7	4.0	3.6	7.0	...	...	...
Industrial production	5.8	10.8	-6	4.4	1.0	1.9	n.a.
Unemployment rate ²	3.7	3.4	3.2	3.3	3.4	3.3	n.a.
Consumer prices ³	2.6	2.1	2.0	2.5	2.4	2.6	2.5
Merch. trade balance ⁴	32.7	29.2	29.5	26.0	23.6	33.1	n.a.
Current account ⁵	15.0	6.1	-6.6	.9	10.1	17.6	n.a.

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate. Imports are c.i.f.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **India**, economic indicators hint at some moderation in output growth after a first-quarter surge. Average industrial production for April and May was up 3.6 percent from the previous quarter. Inflation continued to decline, following monetary policy tightening earlier in the year and other government measures targeted at reducing consumer prices for imported goods, and loan growth slowed. After soaring in April, the trade deficit narrowed a bit in May, as export growth remained strong but imports weakened a touch. The Reserve Bank of India held rates steady at its meeting on July 31 but raised the required cash reserve ratio for banks and removed the ceiling imposed on

the size of its daily reverse repo auctions. Both moves were thought to be targeted at removing liquidity from the banking system related to strong capital inflows.

Indian Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	9.3	8.7	13.1	n.a.	...	...	...
Industrial production	7.9	10.5	3.6	n.a.	-7	1.0	n.a.
Consumer prices ²	5.6	6.5	7.0	5.7	6.7	5.7	4.8
Wholesale prices ²	4.4	5.7	6.4	5.3	6.3	5.4	4.4
Merch. trade balance ³	-44.1	-54.4	-57.6	n.a.	-81.9	-65.8	n.a.
Current account ⁴	-7.8	-9.4	10.3	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent change from year-earlier period, except annual data, which are Dec./Dec.

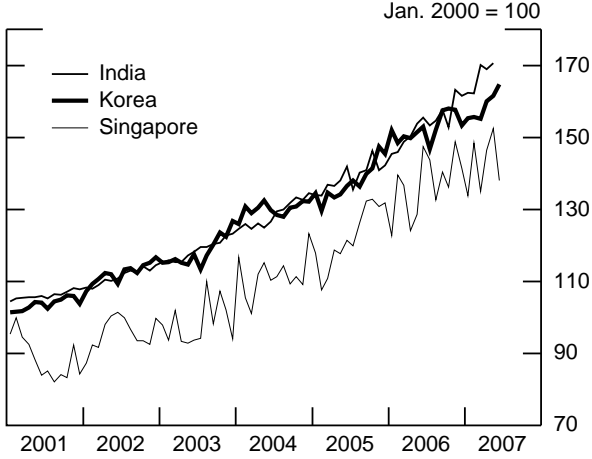
3. Billions of U.S. dollars, annual rate.

4. Billions of U.S. dollars, n.s.a., annual rate.

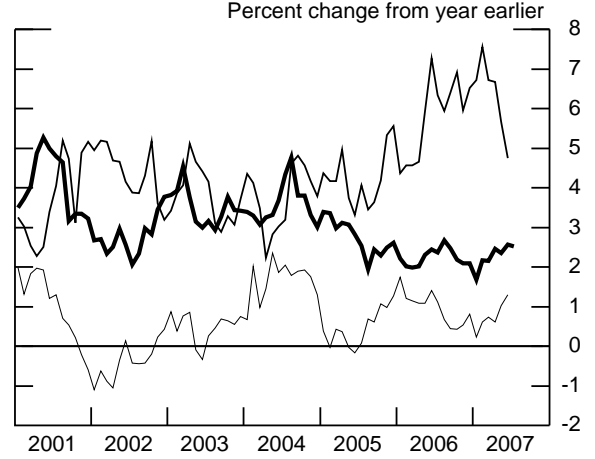
n.a. Not available. ... Not applicable.

India, Korea, and Singapore

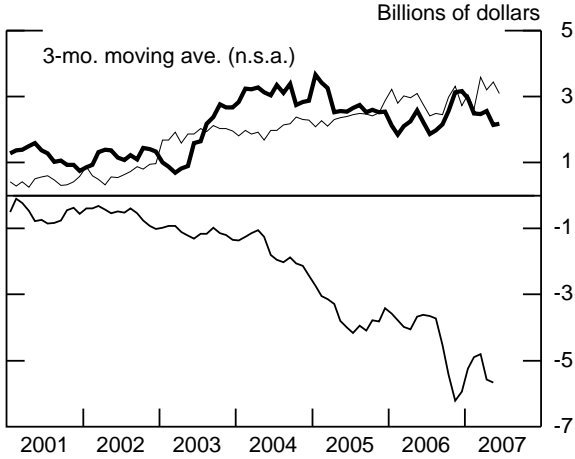
Industrial Production



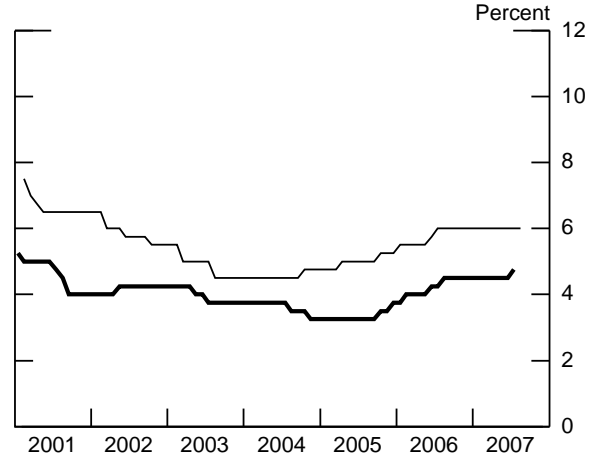
Consumer Prices



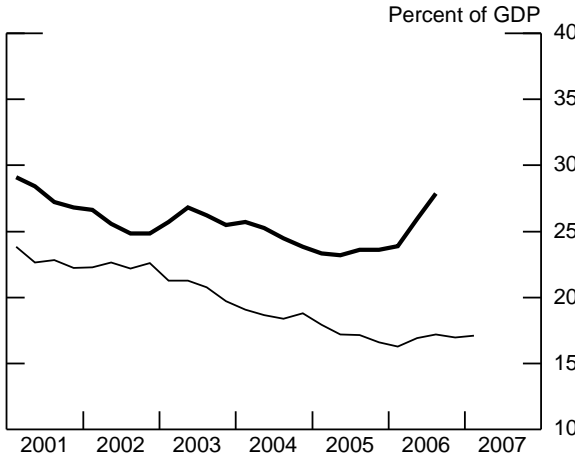
Merchandise Trade Balances



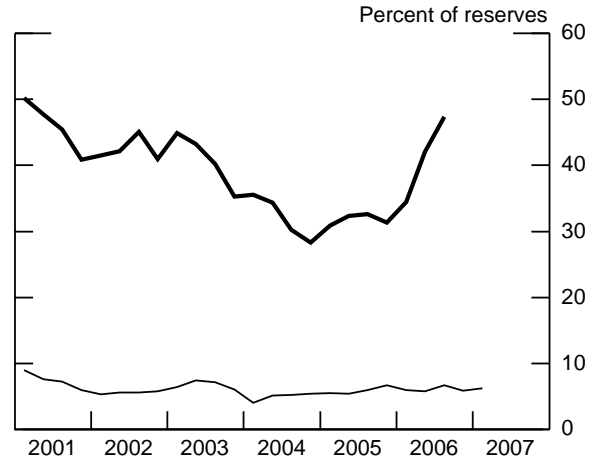
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



Recent data for the **ASEAN** region suggest continued expansion in the second quarter. In Singapore, the advance unofficial estimate (not shown) indicates that second-quarter real GDP rose nearly 13 percent, as the volatile biomedical sector rebounded and domestic activity, notably construction, continued to be strong. Elsewhere in the region, average industrial production for April and May was up from first-quarter levels, and trade surpluses remained high.

Twelve-month consumer price inflation across the region continued to decline in most countries owing to more subdued energy price inflation and, in some countries, the unwinding of previous increases in food prices and local currency appreciation. One exception was Singapore, where higher healthcare and recreation prices boosted headline inflation. Amid the reduced inflationary pressures and the desire to stimulate domestic demand, the central banks of Indonesia and Thailand lowered interest rates 25 basis points in July. The Philippine central bank also lowered its policy rate 150 basis points in mid-July, but the bank simultaneously removed a tiered scheme that offered a lower interest rate on large deposits. The rapid appreciation of its currency against the U.S. dollar prompted Thailand to relax its foreign exchange regulations in order to facilitate capital outflows. Similarly, the Philippine central bank announced that it would ease foreign exchange regulations by the end of September.

ASEAN Economic Indicators: Growth
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
<i>Real GDP¹</i>							
Indonesia	4.9	6.0	3.0	n.a.	...	...	...
Malaysia	5.7	5.8	5.1	n.a.	...	...	...
Philippines	5.6	5.5	10.3	n.a.	...	...	...
Singapore	8.2	6.5	7.6	n.a.	...	...	...
Thailand	4.3	4.2	4.9	n.a.	...	...	...
<i>Industrial production²</i>							
Indonesia ³	1.3	-1.6	1.0	n.a.	3.6	-4	n.a.
Malaysia	4.0	5.1	-2.3	n.a.	1.1	4.0	n.a.
Philippines	2.2	-9.9	-7.4	n.a.	2.3	-1.5	n.a.
Singapore	9.5	11.9	-2.1	4.7	8.5	4.1	-9.4
Thailand	9.1	7.4	1.7	1.6	.0	2.8	-6

1. Annual rate. Annual data are Q4/Q4.

2. Annual data are annual averages.

3. Staff estimate.

n.a. Not available. ... Not applicable.

ASEAN Economic Indicators: Merchandise Trade Balance
(Billions of U.S. dollars, s.a.a.r.)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Indonesia	28.0	39.7	43.1	40.0	43.7	36.8	39.6
Malaysia	26.4	29.5	24.3	n.a.	20.3	30.6	n.a.
Philippines	-6.2	-4.4	.9	n.a.	2.4	-.9	n.a.
Singapore	29.6	33.1	42.9	36.9	45.3	31.8	33.8
Thailand	-8.5	2.2	16.2	13.0	6.7	14.4	18.1

n.a. Not available.

ASEAN Economic Indicators: CPI Inflation
(Percent change from year earlier, except as noted)

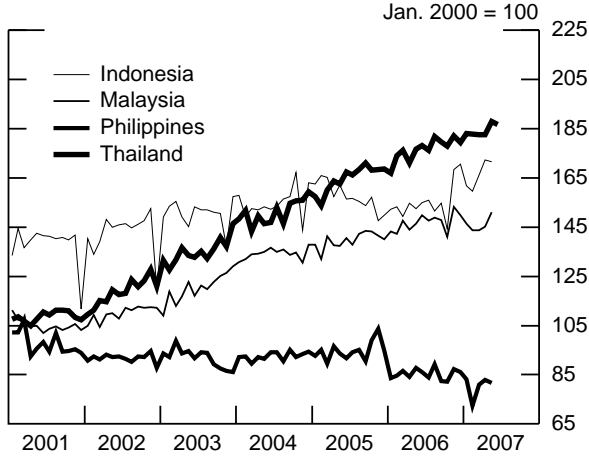
Indicator	2005 ¹	2006 ¹	2007				
			Q1	Q2	May	Jun.	Jul.
Indonesia	17.0	6.7	6.3	6.0	6.1	5.7	6.0
Malaysia	3.3	3.1	2.6	1.5	1.4	1.4	n.a.
Philippines	6.7	4.3	2.9	2.4	2.4	2.3	n.a.
Singapore	1.3	.8	.5	1.0	1.0	1.3	n.a.
Thailand	5.8	3.5	2.5	1.9	1.9	1.9	1.7

1. Dec./Dec.

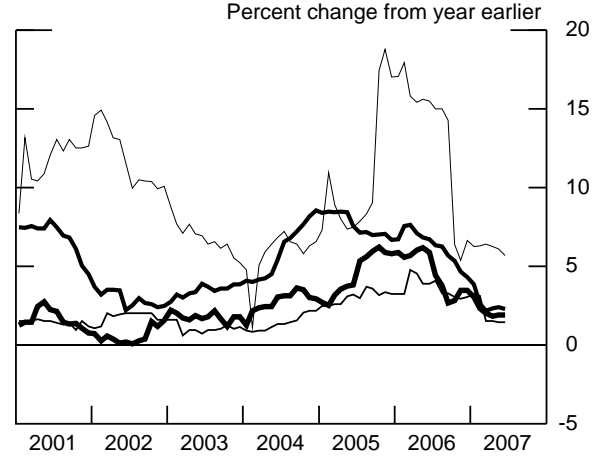
n.a. Not available.

ASEAN-4

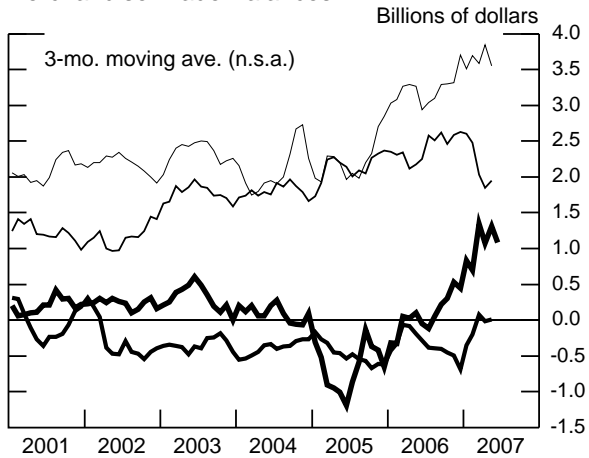
Industrial Production



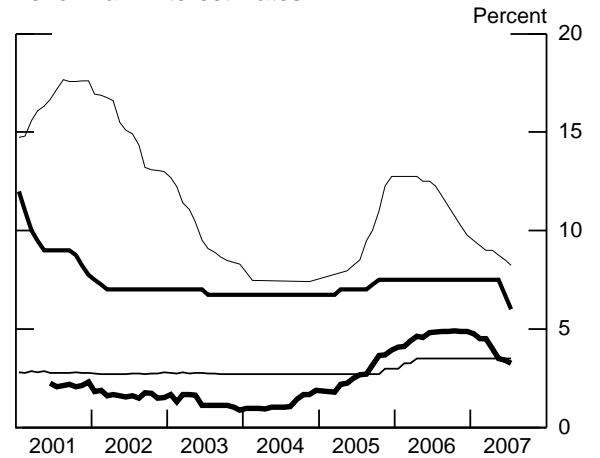
Consumer Prices



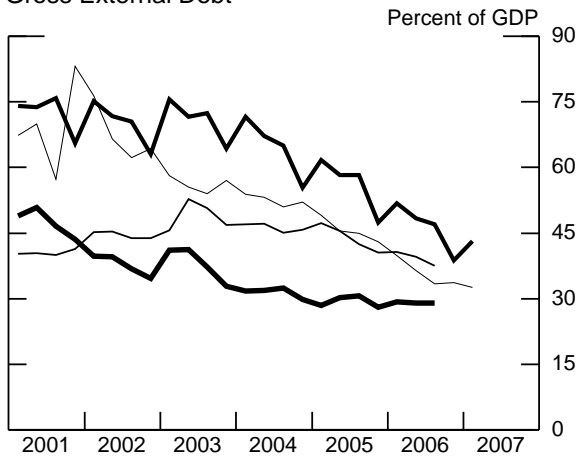
Merchandise Trade Balances



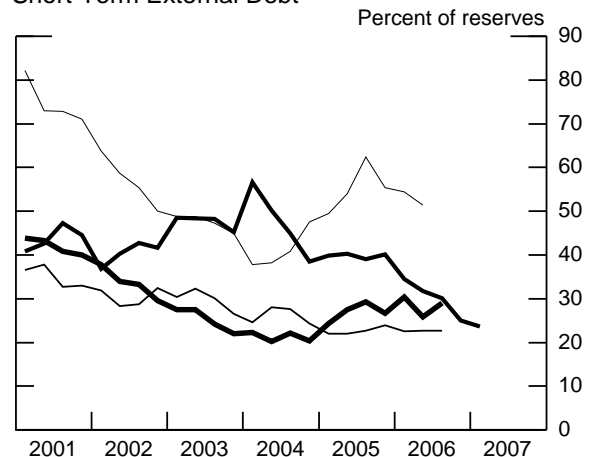
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



In **Mexico**, recent indicators point to a weaker-than-expected rebound in economic activity in the second quarter. The average level of industrial production in April and May was up only 1 percent from the first quarter, as the key manufacturing and construction sectors failed to experience any significant recovery from their first-quarter weakness.

Twelve-month headline inflation remained at 4 percent in June, largely due to increases in milk, avocado, and orange prices. Despite inflation hovering around the upper limit of the Bank of Mexico's 2-to-4 percent inflation target range, the central bank decided during its late July meeting not to tighten monetary policy but signaled a further tightening of policy might occur if inflation does not recede as expected.

Mexican Economic Indicators
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	2.5	4.3	.6	n.a.	...	...	...
Overall economic activity	3.1	4.9	.2	n.a.	.9	.3	n.a.
Industrial production	2.1	5.0	-1.0	n.a.	1.1	.0	n.a.
Unemployment rate ²	3.6	3.6	3.8	3.7	3.7	3.7	3.6
Consumer prices ³	3.3	4.1	4.1	4.0	4.0	4.0	4.0
Merch. trade balance ⁴	-7.6	-6.1	-13.2	-15.6	-16.3	-13.9	-16.6
Merchandise imports ⁴	221.8	256.1	265.1	280.6	276.9	281.1	283.9
Merchandise exports ⁴	214.2	250.0	252.0	265.0	260.6	267.2	267.3
Current account ⁵	-4.9	-1.8	-11.0	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent; counts as unemployed those working one hour a week or less.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Brazil**, recent data releases indicate robust activity in the second quarter. Average April-May industrial production was up 1.7 percent from the first quarter and 4½ percent from a year earlier, while retail sales were up over 9 percent from a year earlier. The trade surplus widened to \$49 billion in the second quarter (a.r.), boosted by high commodities prices, bringing the current account surplus to over \$10 billion, about 1 percent of GDP. The trade surplus narrowed again in July, largely due to an increase in imports.

Twelve-month inflation moved up to 3.8 percent in June, fueled in part by higher prices of food, but is well below the 4.5 percent mid-point of the government's inflation target range. On July 18, the central bank reduced its target for the Selic rate 50 basis points, to 11.5 percent. The central bank continued to intervene to mitigate upward pressures on the *real*, raising international reserves to a record \$155 billion. The capital account surplus in the first half of the year reached nearly \$60 billion, ten times the pace over the same period of 2006, reflecting a rise in both foreign direct investment and net portfolio capital inflows.

Brazilian Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	May	Jun.	Jul.
Real GDP ¹	3.1	4.7	3.1	n.a.	...	...	...
Industrial production	3.1	2.8	1.3	n.a.	1.3	n.a.	n.a.
Unemployment rate ²	9.8	10.0	9.7	9.6	9.7	9.6	n.a.
Consumer prices ³	5.7	3.3	3.1	3.4	3.3	3.8	n.a.
Merch. trade balance ⁴	44.8	46.1	40.7	48.6	47.1	42.0	27.5
Current account ⁵	14.0	13.6	7.0	10.5	1.4	8.3	n.a.

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

Price index is IPCA.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Argentina**, indicators for the second quarter suggest a solid pickup in growth. Industrial production in the second quarter was up 1¾ percent over the first quarter. The merchandise trade surplus in the second quarter also rose, and twelve-month inflation ticked down to 8.8 percent in June. Senator Cristina Kirchner, wife of current President Nestor Kirchner, has officially announced her candidacy for president; President Kirchner decided not to seek reelection despite his popularity. Senator Kirchner is a member of the ruling Peronist Party, and she is currently well ahead in opinion polls. Elections will be held on October 28.

Argentine Economic Indicators
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	8.8	8.7	3.9	n.a.	...	...	...
Industrial production	8.0	8.4	.3	1.8	.3	.6	.0
Unemployment rate ²	11.6	10.2	9.8	n.a.	...	...	...
Consumer prices ³	12.1	9.7	9.4	8.9	8.9	8.9	8.8
Merch. trade balance ⁴	11.7	12.3	7.4	13.1	8.6	8.4	12.3
Current account ⁵	5.7	8.0	3.4	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent; n.s.a.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **Venezuela**, inflation remained very high, ending at over 17 percent in July on a twelve-month basis. The government continued to focus most of its attention on suppressing inflationary pressures, in part by reducing the VAT from 11 to 9 percent in July. The government is also reputed to have lowered spending growth in recent months, but fiscal accounts lack transparency.

In recent weeks, the Finance Minister stated that the official bolívar would not be devalued in January 2008, when a so-called monetary reform is enacted, but may be devalued in early 2009. (In January 2008, the bolívar is scheduled to be replaced by the bolívar fuerte, which will be equal to 1,000 bolívares.) The parallel market bolívar has depreciated 25 percent against the dollar over the past nine months, fueling inflationary pressures, and prompting congressional efforts to punish those who have large transactions in the market. At the end of July, the parallel market exchange rate stood at over 4,200 bolívares per dollar, versus 2,144 per dollar for the official rate. The government also continued to conduct intervention sales of foreign exchange to support the bolívar via non-market mechanisms. On July 27, the central bank's international reserves including gold stood at about \$25 billion, down from \$30 billion at end 2006.

Venezuelan Economic Indicators
(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	May	Jun.	Jul.
Real GDP ¹	10.9	11.8	-2.3	n.a.	...	...	...
Unemployment rate ²	12.2	10.0	9.8	8.2	8.0	8.2	n.a.
Consumer prices ³	14.4	17.0	19.1	19.5	19.6	19.4	17.2
Non-oil trade balance ⁴	-14.3	-22.7	-30.6	n.a.	...	...	...
Merch. trade balance ⁴	31.8	33.0	18.1	n.a.	...	...	...
Current account ⁵	25.5	27.2	14.6	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent.

3. Percent change from year-earlier period, except annual data, which are Dec./Dec.

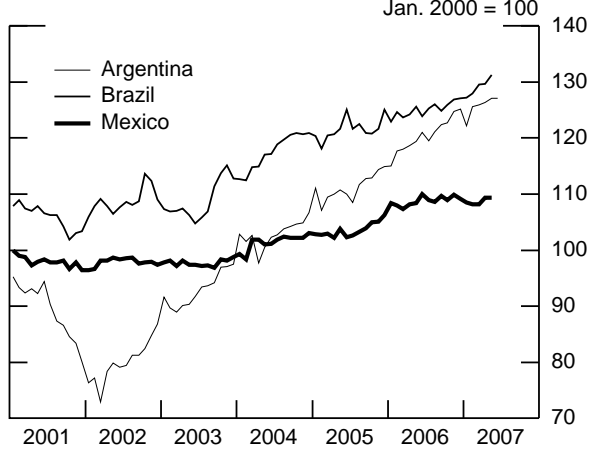
4. Billions of U.S. dollars, annual rate.

5. Billions of U.S. dollars, n.s.a., annual rate.

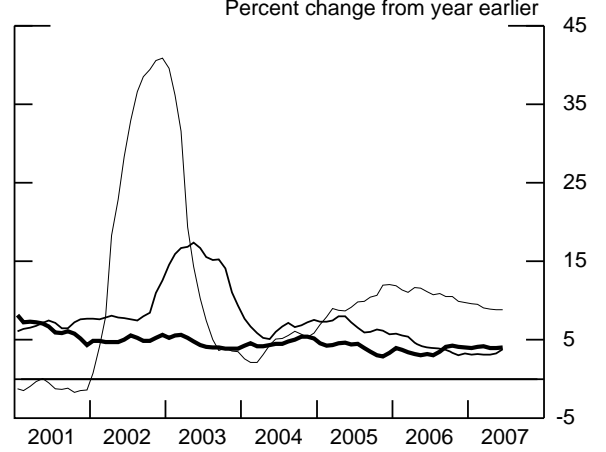
n.a. Not available. . . . Not applicable.

Latin America

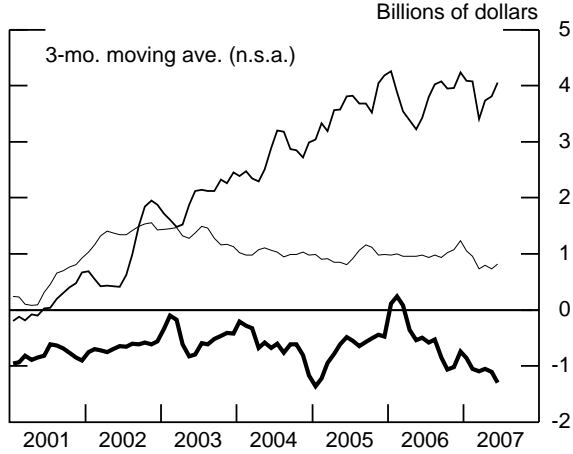
Industrial Production



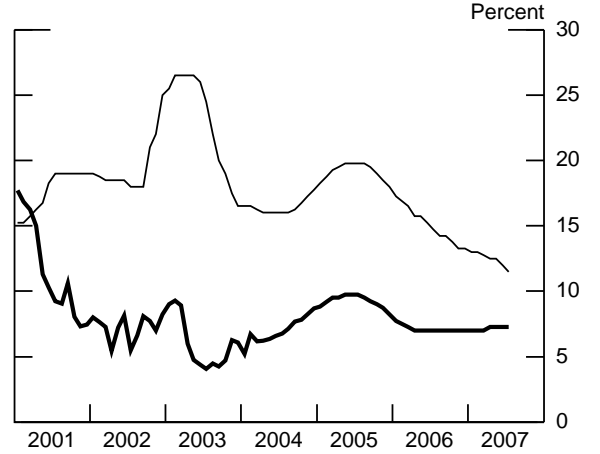
Consumer Prices



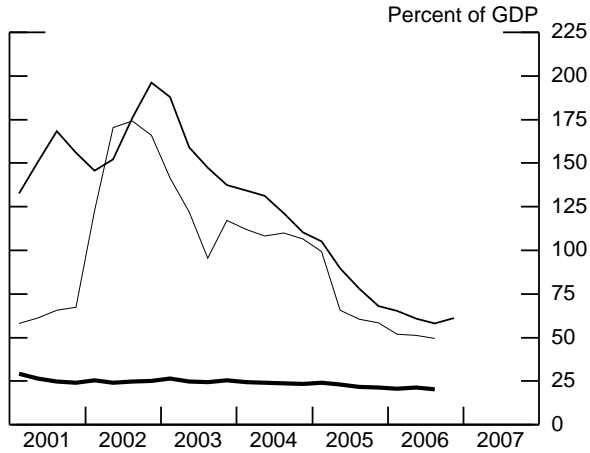
Merchandise Trade Balances



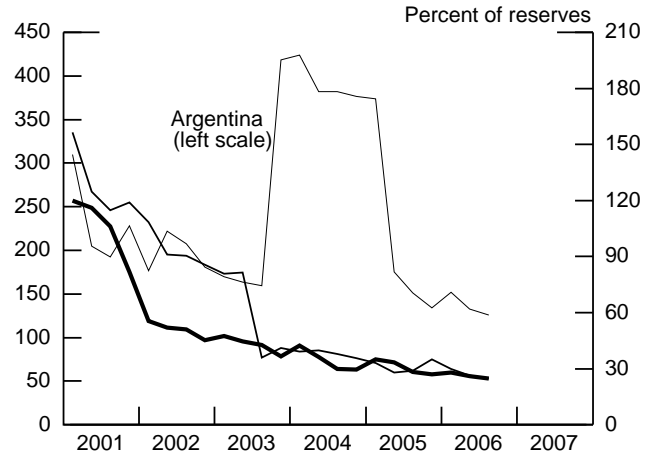
Benchmark Interest Rates



Gross External Debt



Short-Term External Debt



In **Turkey**, real GDP expanded 6.8 percent in the first quarter, on the back of strong growth in government consumption and net exports, and the unemployment rate decreased slightly. However, the large current account deficit widened despite strong growth in exports. Industrial production rose 3.5 percent in May after weakness earlier in the year.

Twelve-month consumer price inflation continued to edge down in June but remained well above the central bank's 2007 target of 4 percent. Early results from the recent parliamentary election indicate the ruling AK Party will remain in power, as expected. Financial markets reacted favorably to the results as investors anticipated the AK Party would press ahead with its pro-business reform agenda. EU accession talks continue, although progress on several critical chapters has stalled.

Turkish Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	7.4	6.1	6.8	n.a.	...	...	...
Industrial production	5.4	5.9	.6	n.a.	-1.3	3.5	n.a.
Consumer prices ²	7.7	9.7	10.3	9.5	10.7	9.2	8.6
Merch. trade balance ³	-43.3	-52.8	-54.0	-60.1	-52.8	-63.1	-64.2
Current account ⁴	-22.6	-31.9	-36.7	n.a.	-37.8	-42.0	n.a.
Unemployment rate	10.2	9.8	9.7	n.a.	...	...	...

1. Percent change from year-earlier period. Annual data are annual averages.

2. Percent change from year-earlier period, except annual data, which are Dec./Dec.

3. Billions of U.S. dollars, annual rate. Imports are c.i.f.

4. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.

In **South Africa**, indicators on second-quarter performance were mixed. Manufacturing recovered strongly in May, though production in the mining sector was down. Because of high commodity prices, the value of metal exports reached a record level in May, leading to an improvement in the merchandise trade balance. However, the trade balance worsened again in July as exports fell while imports increased. Twelve-month consumer price inflation in June was 6.4 percent, making June the third consecutive month in which prices have breached the South African Reserve Bank's 3-6 percent target range. The sources of inflation are widespread, but food and fuel prices made a combined contribution of 3.7 percentage points. The outlook for inflation has worsened somewhat

as public-sector strikes in June were resolved with employees receiving a 7.5 percent cost-of-living raise.

South African Economic Indicators

(Percent change from previous period, s.a., except as noted)

Indicator	2005	2006	2007				
			Q1	Q2	Apr.	May	Jun.
Real GDP ¹	4.9	5.2	4.7	n.a.	...	...	...
Manuf. production	3.6	4.8	1.3	n.a.	-2.2	4.5	n.a.
Mining production	1.3	-1.6	-2.9	n.a.	.6	-1.5	n.a.
Consumer prices ²	3.9	4.6	5.2	6.4	6.3	6.4	6.4
Merch. trade balance ³	-3.0	-9.6	-9.3	-7.4	-5.6	-2.1	-14.4
Current account ⁴	-9.7	-16.5	-15.0	n.a.	...	...	...

1. Annual rate. Annual data are Q4/Q4.

2. Percent change from year-earlier period for the CPIX, except annual data, which are Dec./Dec. CPIX excludes interest rates on mortgage bonds.

3. Billions of U.S. dollars, annual rate.

4. Billions of U.S. dollars, n.s.a., annual rate.

n.a. Not available. ... Not applicable.